INFORMATION CONTAINED IN THIS PROSPECTUS SUPPLEMENT IS SUBJECT TO COMPLETION PURSUANT TO RULE 424 UNDER THE SECURITIES ACT OF 1933. A REGISTRATION STATEMENT RELATING TO THESE SECURITIES HAS BEEN DECLARED EFFECTIVE BY THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO RULE 415 UNDER THE SECURITIES ACT OF 1933. A FINAL PROSPECTUS SUPPLEMENT AND PROSPECTUS WILL BE DELIVERED TO PURCHASERS OF THESE SECURITIES. THIS PROSPECTUS SUPPLEMENT AND THE PROSPECTUS SHALL NOT CONSTITUTE AN OFFER TO SELL OR THE SOLICITATION OF AN OFFER TO BUY NOR SHALL THERE BE ANY SALE OF THESE SECURITIES IN ANY STATE IN WHICH SUCH OFFER, SOLICITATION OR SALE WOULD BE UNLAWFUL PRIOR TO REGISTRATION OR QUALIFICATION UNDER THE SECURITIES LAWS OF ANY SUCH STATE.

SUBJECT TO COMPLETION
PRELIMINARY PROSPECTUS SUPPLEMENT DATED JUNE 7, 1995

PROSPECTUS SUPPLEMENT
(TO PROSPECTUS DATED MARCH 23, 1994)

$100,000,000

[LOGO]

# % CONVERTIBLE SENIOR DEBENTURES DUE 2005

The % Convertible Senior Debentures due 2005 (the "Debentures") of Alaska Air Group, Inc. ("Air Group" or the "Company") are convertible at any time prior to maturity, unless previously redeemed, into shares of the Company's Common Stock at a conversion price of $ per share (equivalent to a conversion rate of shares per $1,000 principal amount of Debentures), subject to certain adjustments. The Common Stock is listed on the New York Stock Exchange under the symbol "ALK". On June 6, 1995, the last reported sales price of the Common Stock on the New York Stock Exchange was $16 per share.

Interest on the Debentures is payable on June 15 and December 15 of each year, commencing December 15, 1995. The Debentures are redeemable at the Company's option, in whole or in part, at any time on or after June 15, 1998, at the redemption prices set forth herein. In the event of a Change in Control (as hereinafter defined), each holder of the Debentures may require the Company to repurchase all or a portion of such holder's Debentures at 100% of the principal amount thereof, together with accrued and unpaid interest, if any, to the date of repurchase. See "Description of the Debentures."

The Debentures will constitute senior unsecured obligations of the Company and will rank PARI PASSU in right of payment to the Company's other senior unsecured indebtedness. See "Capitalization" and "Description of the Debentures." The Company is a holding company and, accordingly, the Debentures will be effectively subordinated to all existing and future liabilities of the Company's operating subsidiaries.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION, NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS SUPPLEMENT OR THE PROSPECTUS TO WHICH IT RELATES. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

| | PRICE TO PUBLIC (1) | UNDERWRITING DISCOUNT (2) | PROCEEDS TO COMPANY (1)(3) |
|---|---|---|---|
| Per Debenture.............................. | % | % | % |
| Total (4)................................. | $ | $ | $ |

<FN>
(1) Plus accrued interest, if any, from date of issuance.
(2) The Company has agreed to indemnify the several Underwriters against certain liabilities under the Securities Act of 1933, as amended. See

"Underwriting."
(3) Before deducting expenses payable by the Company estimated at $ .
(4) The Company has granted the several Underwriters an option, exercisable within 30 days after the date of this Prospectus Supplement, to purchase up to an additional $15,000,000 aggregate principal amount of Debentures on the terms set forth above to cover over-allotments, if any. If such option is exercised in full, the total Price to Public, Underwriting Discount and Proceeds to Company will be $ , $ and $ , respectively. See "Underwriting."

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The Debentures are offered by the several Underwriters, subject to prior sale, when, as and if issued to and accepted by them, subject to approval of certain legal matters by counsel for the Underwriters and certain other conditions. The Underwriters reserve the right to withdraw, cancel or modify such offer and to reject orders in whole or in part. It is expected that delivery of the Debentures will be made in New York, New York on or about , 1995.

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MERRILL LYNCH & CO. GOLDMAN, SACHS & CO.

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The date of this Prospectus Supplement is , 1995.

[MAP INDICATING ALASKA AIRLINES AND HORIZON AIR ROUTES]

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE DEBENTURES OFFERED HEREBY AND OF THE OUTSTANDING COMMON STOCK OF THE COMPANY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH TRANSACTIONS MAY BE EFFECTED ON THE NEW YORK STOCK EXCHANGE OR OTHERWISE. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.



## PROSPECTUS SUPPLEMENT SUMMARY

THE FOLLOWING SUMMARY IS QUALIFIED IN ITS ENTIRETY BY THE DETAILED INFORMATION AND CONSOLIDATED FINANCIAL STATEMENTS INCLUDED ELSEWHERE HEREIN OR INCORPORATED BY REFERENCE INTO THIS PROSPECTUS SUPPLEMENT AND THE ACCOMPANYING PROSPECTUS. THIS PROSPECTUS SUPPLEMENT SHOULD BE READ IN CONJUNCTION WITH THE ACCOMPANYING PROSPECTUS DATED MARCH 23, 1994.

### THE COMPANY

Air Group is a holding company incorporated in Delaware in 1985. Its principal subsidiaries are Alaska Airlines, Inc. ("Alaska Airlines") and Horizon Air Industries, Inc. ("Horizon"). Alaska Airlines, founded in 1932, provides scheduled air transportation to 37 cities in Alaska, Washington, Oregon, Nevada, California and Arizona, three cities in Mexico, three cities in the Russian Far East and many smaller communities in Alaska and California through code-sharing agreements with local carriers. As of December 31, 1994, Alaska Airlines operated 23 owned and 49 leased jet aircraft with an average age of six years. Horizon, a regional commuter carrier founded in 1981, provides scheduled air transportation to 36 cities in Washington, Oregon, Montana, Idaho and California, as well as two cities in Canada. Horizon provides interconnecting passenger traffic to Alaska Airlines through its major hub cities, Seattle, Portland and Spokane. As of December 31, 1994, Horizon operated five owned and 60 leased aircraft with an average age of nine years.

For the year ended December 31, 1994, Air Group's consolidated operating revenues were $1.3 billion, of which 89% came from scheduled passenger services, 7% came from freight and mail, and 4% came from mileage plan partners and other nonpassenger sources. Alaska Airlines carried approximately 9.0 million passengers in 1994 and accounted for approximately 81% of Air Group's consolidated 1994 operating revenues. Horizon carried approximately 3.5 million passengers in 1994 and accounted for the remaining 19% of Air Group's consolidated 1994 operating revenues.

The Company's strategy is to define strategic markets and then to achieve strong market positions by offering high-quality service at competitive prices. The combined route system of Alaska Airlines and Horizon, when viewed as a whole, blends aspects of both the hub-and-spoke and linear route system concepts, resulting in an integrated system that provides passengers with more frequent flights than the Company's competitors in a substantial majority of the 150 nonstop city pairs that the Company serves. Both Alaska Airlines and Horizon seek to differentiate themselves from their competitors by offering superior levels of value and service. Alaska Airlines' service has been recognized with a number of awards, including Airline of the Year awards from CONDE NAST TRAVELER magazine in five of the last six years and high rankings in consumer magazines and customer surveys by J.D. Power & Associates and the Zagat's United States Travel Survey.

## THE OFFERING

| | |
|---|---|
| Issue | $100,000,000 principal amount of % Convertible Senior Debentures due 2005. |
| Interest | Each Debenture will bear interest at a rate of % per annum. Interest will be paid semiannually on June 15 and December 15 of each year, commencing December 15, 1995. See "Description of the Debentures--General" in this Prospectus Supplement. |
| Conversion Rights | Each Debenture will be convertible, at the holder's option, at any time on or prior to maturity, unless previously redeemed or otherwise purchased, into Common Stock at a conversion price of $ per share (equivalent to a conversion rate of shares per $1,000 principal amount of Debentures), subject to certain adjustments. See "Description of the Debentures-- Conversion" in this Prospectus Supplement. |



| | |
|---|---|
| Optional Redemption | The Debentures will be redeemable, in whole or in part, at the Company's option at any time on or after June 15, 1998, initially at % of their principal amount, plus accrued interest, declining to 100% of their principal amount, plus accrued interest, on or after June 15, 2004. See "Description of the Debentures--Redemption" in this Prospectus Supplement. |
| Purchase of Debentures Upon a Change in Control | At the holder's option, the Company will purchase for cash any Debenture, as of 35 business days after the occurrence of a Change in Control of the Company, for a Change in Control Purchase Price equal to 100% of the principal amount thereof, plus accrued and unpaid interest, if any, to the Change in Control Purchase Date. The Change in Control purchase feature of the Debentures may in certain circumstances have an antitakeover effect. See "Description of the Debentures--Purchase of Debentures Upon a Change in Control" in this Prospectus Supplement for a summary of these provisions and the definitions of the above defined terms. |
| Ranking | The Debentures will constitute senior unsecured obligations of Air Group and will rank PARI PASSU in right of payment to Air Group's other senior unsecured indebtedness. See "Description of the Debentures--Ranking" in this Prospectus Supplement. Air Group is a holding company and, accordingly, the Debentures will be effectively subordinated to all |

| | |
|---|---|
| | existing and future liabilities of Air Group's operating subsidiaries, including Alaska Airlines and Horizon. |
| Use of Proceeds.................. | The net proceeds to the Company from this offering will be added to working capital and used for general corporate purposes, including the redemption or repurchase of the Company's outstanding 7 1/4% zero coupon convertible subordinated notes due 2006. Pending such uses, the net proceeds of this offering will be invested in short-term, interest-bearing securities. See "Use of Proceeds" in this Prospectus Supplement. |



## SUMMARY FINANCIAL AND OPERATING DATA

The following table summarizes selected financial and operating information for Air Group and its principal subsidiaries, Alaska Airlines and Horizon. The consolidated financial data for each of the five years ended December 31, 1994, set forth below, have been taken from the financial data included in Air Group's Form 10-K for the year ended December 31, 1994 incorporated by reference in this Prospectus Supplement and the related Registration Statement. The financial statements for the five years ended December 31, 1994 have been examined by Arthur Andersen LLP, independent public accountants. This summary should be read in conjunction with the financial statements, including the notes thereto, and other information contained in the documents incorporated by reference. The selected financial information for the three month periods ended March 31, 1995 and 1994 is unaudited but includes all adjustments (consisting only of normal recurring adjustments) that are necessary, in the opinion of management, for a fair presentation of results of operations for such periods. The airline business is seasonal in nature and the operating results for the three months ended March 31, 1995 are not necessarily indicative of results to be expected for the full year.

| | THREE MONTHS ENDED MARCH 31, | |
|---|---|---|
| | 1995 | 1994 |
| | (DOLLARS IN THOUSANDS) | |
| CONSOLIDATED FINANCIAL DATA: | | |
| STATEMENT OF OPERATIONS DATA: | | |
| Operating revenues...................... | $ 294,573 | $ 280,382 |
| Operating expenses...................... | 312,874 | 283,310 |
| Operating income (loss)................. | (18,301) | (2,928) |
| Net income (loss)....................... | $ (16,340) | $ (6,313) |
| Average primary shares outstanding (000)................................ | 13,400 | 13,349 |
| Primary earnings (loss) per share (a)... | $ (1.22) | $ (0.47) |
| Fully diluted earnings per share........ | (b) | (b) |
| BALANCE SHEET DATA (AT END OF PERIOD): | | |
| Total assets............................ | $1,287,833 | $1,191,587 |
| Long-term debt and capital lease obligations............................ | 579,236 | 593,405 |
| Redeemable preferred stock.............. | -- | -- |
| Shareholders' equity.................... | 175,313 | 160,919 |
| ALASKA AIRLINES OPERATING DATA (C): | | |
| Revenue passenger miles (000,000)....... | 1,793 | 1,536 |
| Available seat miles (000,000).......... | 3,182 | 2,553 |
| Revenue passenger load factor........... | 56.4% | 60.2% |
| Yield per passenger mile................ | 11.2 CENTS | 12.8 CENTS |
| Operating expenses per available seat mile................................... | 7.8 CENTS | 8.9 CENTS |
| HORIZON AIR OPERATING DATA (C): | | |
| Revenue passenger miles (000,000)....... | 186 | 143 |
| Available seat miles (000,000).......... | 323 | 241 |
| Revenue passenger load factor........... | 57.7% | 59.4% |
| Yield per passenger mile................ | 31.9 CENTS | 35.7 CENTS |
| Operating expenses per available seat mile................................... | 20.6 CENTS | 22.9 CENTS |

| | YEAR ENDED DECEMBER 31, | | | | |
|---|---|---|---|---|---|
| | 1994 | 1993 | 1992 | 1991 | 1990 |
| CONSOLIDATED FINANCIAL DATA: | | | | | |
| STATEMENT OF OPERATIONS DATA: | | | | | |
| Operating revenues...................... | $1,315,620 | $1,128,329 | $1,115,378 | $1,104,031 | $1,046,965 |
| Operating expenses...................... | 1,240,622 | 1,145,102 | 1,210,219 | 1,069,405 | 1,018,546 |
| Operating income (loss)................. | 74,998 | (16,773) | (94,841) | 34,626 | 28,419 |
| Net income (loss)....................... | $ 22,531 | $ (30,918) | $ (84,837) | $ 10,338 | $ 17,167 |

| | | | | | |
|---|---|---|---|---|---|
| Average primary shares outstanding (000) | 13,378 | 13,340 | 13,309 | 13,413 | 13,675 |
| Primary earnings (loss) per share (a) | $ 1.68 | $ (2.51) | $ (6.87) | $ 0.27 | $ 0.82 |
| Fully diluted earnings per share | 1.62 | (b) | (b) | (b) | (b) |
| BALANCE SHEET DATA (AT END OF PERIOD): | | | | | |
| Total assets | $1,315,771 | $1,134,954 | $1,208,358 | $1,225,455 | $1,021,404 |
| Long-term debt and capital lease obligations | 589,904 | 525,418 | 487,847 | 499,971 | 281,759 |
| Redeemable preferred stock | -- | -- | 61,235 | 60,947 | 60,665 |
| Shareholders' equity | 191,278 | 166,833 | 196,724 | 284,447 | 279,833 |
| ALASKA AIRLINES OPERATING DATA (C): | | | | | |
| Revenue passenger miles (000,000) | 7,587 | 5,514 | 5,537 | 4,948 | 4,494 |
| Available seat miles (000,000) | 12,082 | 9,426 | 9,617 | 8,789 | 8,380 |
| Revenue passenger load factor | 62.8% | 58.5% | 57.6% | 56.3% | 53.6% |
| Yield per passenger mile | 12.2 CENTS | 14.3 CENTS | 14.5 CENTS | 16.7 CENTS | 17.8 CENTS |
| Operating expenses per available seat mile | 8.3 CENTS | 9.9 CENTS | 10.5 CENTS | 10.2 CENTS | 10.3 CENTS |
| HORIZON AIR OPERATING DATA (C): | | | | | |
| Revenue passenger miles (000,000) | 733 | 560 | 486 | 405 | 357 |
| Available seat miles (000,000) | 1,165 | 986 | 905 | 786 | 720 |
| Revenue passenger load factor | 62.9% | 56.8% | 53.7% | 51.5% | 49.6% |
| Yield per passenger mile | 33.3 CENTS | 37.9 CENTS | 40.7 CENTS | 42.9 CENTS | 43.4 CENTS |
| Operating expenses per available seat mile | 21.0 CENTS | 21.8 CENTS | 22.2 CENTS | 22.3 CENTS | 21.9 CENTS |

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(a) For 1992, primary earnings per share includes $(.34) for the $4.6 million cumulative effect of the postretirement benefits accounting change as of January 1, 1992.
(b) Antidilutive.
(c) See "Selected Financial and Operating Data" for definition of terms.



## THE COMPANY

Air Group is a holding company incorporated in Delaware in 1985. Its principal subsidiaries are Alaska Airlines and Horizon. Alaska Airlines, founded in 1932, provides scheduled air transportation to 37 cities in Alaska, Washington, Oregon, Nevada, California and Arizona, three cities in Mexico, three cities in the Russian Far East and many smaller communities in Alaska and California through code-sharing agreements with local carriers. As of December 31, 1994, Alaska Airlines operated 23 owned and 49 leased jet aircraft with an average age of six years. Horizon, a regional commuter carrier founded in 1981, provides scheduled air transportation to 36 cities in Washington, Oregon, Montana, Idaho and California, as well as two cities in Canada. Horizon provides interconnecting passenger traffic to Alaska Airlines through its major hub cities, Seattle, Portland and Spokane. As of December 31, 1994, Horizon operated five owned and 60 leased aircraft with an average age of nine years.

For the year ended December 31, 1994, Air Group's consolidated operating revenues were $1.3 billion, of which 89% came from scheduled passenger services, 7% came from freight and mail, and 4% came from mileage plan partners and other nonpassenger sources. Alaska Airlines carried approximately 9.0 million passengers in 1994 and accounted for approximately 81% of Air Group's consolidated 1994 operating revenues. Horizon carried approximately 3.5 million passengers in 1994 and accounted for the remaining 19% of Air Group's consolidated 1994 operating revenues.

The Company's strategy is to define strategic markets and then to achieve strong market positions by offering high-quality service at competitive prices. The combined route system of Alaska Airlines and Horizon, when viewed as a whole, blends aspects of both the hub-and-spoke and linear route system concepts, resulting in an integrated system that provides passengers more frequent flights than the Company's competitors in a substantial majority of the 150 nonstop city pairs that the Company serves. Both Alaska Airlines and Horizon seek to differentiate themselves from their competitors by offering superior levels of value and service. Alaska Airlines' service has been recognized with a number of awards, including Airline of the Year awards from CONDE NAST TRAVELER magazine in five of the last six years and high rankings in consumer magazines and customer surveys by J.D. Power & Associates and the Zagat's United States

Travel Survey.

COST AND PRODUCTIVITY IMPROVEMENTS

In response to changing conditions and intense competition, Alaska Airlines executed a cost reduction and productivity improvement program beginning in 1992 and continuing into 1995. As a result of this program, Alaska Airlines has been able to significantly reduce its cost per available seat mile ("ASM") from 10.2 cents in 1992 to 8.3 cents in 1994 and to 7.8 cents in the first quarter of 1995. The program embodies the following five key elements:

- Achieving permanent reductions in operating costs

- Improving productivity of equipment

- Improving productivity of employees

- Reducing or eliminating unprofitable flights

- Restructuring the Company's finances to reduce high-cost debt and lease expense

OPERATING COST REDUCTION. Management reviewed and evaluated every Company program to eliminate nonessential activities. Vendor contracts were renegotiated, operating procedures revised, and staffing levels reduced. Without compromising quality, Alaska Airlines and Horizon reduced their inflight meal costs by altering menus, emphasizing lighter fare, and discontinuing meals on shorter flights and on those flights operating outside of regular mealtimes. Alaska Airlines and Horizon are currently developing an electronic ticketing program, as well as other more direct methods for ticket distribution, which are expected to offer improved customer convenience and may reduce distribution costs.

FLEET PRODUCTIVITY. Recognizing the cost savings that could be achieved by operating a more efficient fleet, Alaska Airlines undertook a targeted program of aircraft retirement. Since 1992, Alaska Airlines has



retired 25 older Boeing 727-200/100 aircraft while adding 33 new McDonnell Douglas MD-80 and Boeing 737-400 aircraft, which has resulted in significant fuel, labor and maintenance cost savings. The new aircraft are 33%-45% more fuel efficient and have contributed to lower labor costs since they require only two pilots, compared to the three required by the older aircraft.

While cost reductions were the centerpiece of operating improvements in 1993, productivity improvements were the focus in 1994. By reducing turn times and increasing the workday, Alaska Airlines increased aircraft utilization, measured in block hours per day per aircraft, from 8.5 hours in 1992 to 10.3 hours in 1994 and to 10.4 hours in the first quarter of 1995.

EMPLOYEE PRODUCTIVITY. Alaska Airlines has also found ways to significantly improve employee productivity. From 1992 to 1994, employees per departure improved 12.8%, passengers per employee increased 44.0% and ASMs per employee grew 26.2%. During the same period, Horizon also showed increases in ASMs per employee and passengers per employee.

IMPROVED PROFITABILITY OF ROUTE STRUCTURE. Alaska Airlines reviewed its route structure to identify nonprofitable flights. Service to Boise, Spokane, Tucson, Long Beach, Guadalajara and Mexico City was suspended. Marginal routes were pared, and aircraft were reassigned to core routes in Alaska and California. The Company also continued to explore new opportunities to expand its markets. Service was added to Las Vegas, Reno, Sacramento and a number of smaller communities in Alaska.

FINANCIAL RESTRUCTURING. The Company took advantage of historically low interest rates to restructure its higher-cost obligations. $61.2 million of the Company's preferred stock was redeemed in 1993, thereby eliminating preferred dividends and reducing the Company's after-tax capital costs by more than $4 million per year. In addition, the Company further reshaped its cost structure by entering into an agreement in late 1994 with International Lease Finance Corporation that provides lower ownership costs for 20 of Alaska Airlines' 22 Boeing 737-400 aircraft. This new agreement is expected to generate savings of more than $6 million annually over its 10-year term.

MARKET SHARE

ALASKA AIRLINES

During the first quarter of 1995, Alaska Airlines had the highest share of nonstop flights along its routes in each of its following major markets:

| PACIFIC NORTHWEST TO ALASKA | | WEST COAST U.S. TO WEST COAST MEXICO | |
|---|---|---|---|
| ALASKA AIRLINES | 61.0% | ALASKA AIRLINES | 52.9% |
| MarkAir (1) | 15.0% | Delta | 13.7% |
| Delta | 9.4% | AeroMexico | 13.7% |
| United | 5.4% | Mexicana | 12.8% |
| All Others | 9.2% | Aero California | 6.9% |

| PACIFIC NORTHWEST TO NORTHERN CALIFORNIA | | PACIFIC NORTHWEST TO SOUTHERN CALIFORNIA | |
|---|---|---|---|
| ALASKA AIRLINES | 41.5% | ALASKA AIRLINES | 72.1% |
| United/United Shuttle | 32.4% | United/United Shuttle | 14.6% |
| Southwest | 16.3% | Delta | 10.1% |
| Reno Air | 5.0% | MarkAir (1) | 3.1% |
| All Others | 4.8% | All Others | .1% |

Source: Official Airline Guide Standard Scheduling Information Manual dated May 4, 1995.

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(1) MarkAir has since ceased operating in these markets. See "Recent Operating Results and Developments."



Approximately 65% of Alaska Airlines' passengers travel from the Pacific Northwest to other West Coast destinations, 25% travel between the Pacific Northwest and Alaska or within Alaska, and 10% travel internationally. The most significant element of Alaska Airlines' route system is its high frequency service in all the major West Coast markets that it serves.

Alaska Airlines provides extensive service between the Pacific Northwest and both the Northern California and Southern California markets, as well as within the Pacific Northwest region. Less than three percent of Alaska Airlines' service is on intra-California routes.

Over half of the U.S. cities served by Alaska Airlines are located in the state of Alaska. In each year since 1973, Alaska Airlines has carried more passengers between Alaska and the U.S. mainland than any other airline. Alaska Airlines also serves many smaller communities in Alaska and California through code-sharing agreements with local carriers.

Alaska Airlines serves three resort cities in Mexico: Puerta Vallarta, Mazatlan and Los Cabos. Traffic in these markets is strongest during the winter months, which partially offsets the reduced seasonal demand in Alaska, thereby allowing the Company to better utilize its aircraft fleet. Alaska Airlines serves the Russian Far East with flights to Magadan, Khabarovsk and Vladivostok, and plans to begin service this summer to Petropavlosk.

HORIZON

Horizon is the largest regional airline in the Pacific Northwest, and serves 36 cities in Washington, Oregon, Montana, Idaho and California, as well as two cities in Canada. In 1994, Horizon carried approximately 3.5 million passengers.

Horizon flights are listed under the Alaska Airlines designator code in airline computer reservation systems. Certain Horizon flights are also listed under the Northwest designator code. In 1994, 24% of Horizon's passengers connected to Alaska Airlines flights and another 8% connected to Northwest Airlines flights. The number of passengers connecting between Alaska Airlines and Horizon rose 44% in 1994. In contrast to most regional airlines, Horizon relies much less on connecting traffic, with over half of its passengers having origins and destinations within the Horizon route system.

SERVICE

The Company generally offers the same low fares as its competitors, but with more frequent service. The Company, however, believes that both Alaska Airlines and Horizon offer superior value to their customers by providing a higher level of customer service and amenities as compared to their major competitors. Unlike its major competitors, Alaska Airlines continues to offer meal service, advance seat selection and a first-class cabin. Additionally, Alaska Airlines' fleet, with an average age of six years, is the youngest of any major U.S. carrier and is configured to create more legroom for its passengers. The Company also provides interline services that allow passengers to be ticketed and to check their baggage to their final destinations on virtually every major airline in the world.

The Company's mileage program allows customers to earn mileage credits while flying on Alaska Airlines, as well as Horizon, Northwest Airlines, TWA, SAS, Qantas and British Airways. Mileage credit can be redeemed for travel on Alaska Airlines, Horizon or any of the program partners for reward travel worldwide. Mileage can also be earned from marketing partners such as credit card issuers, long-distance telecommunications carriers, hotels and car rental firms. In 1994, the Company generated $34 million in revenues from sales of mileage credits to nonairline partners.

EMPLOYEES

Alaska Airlines had 6,901 full-time and part-time employees as of December 31, 1994, approximately 87% of whom are represented under collective bargaining agreements. No material Alaska Airlines labor agreements are amendable until September 1997.

Horizon had 2,951 full-time and part-time employees as of December 31, 1994, approximately 20% of whom are represented under collective bargaining agreements.



USE OF PROCEEDS

The net proceeds to the Company from the sale of the Debentures offered hereby are estimated to be approximately $ (excluding expenses other than the Underwriters' discount and assuming that the Underwriters' over-allotment option is not exercised). Such net proceeds will be added to working capital and used for general corporate purposes, including the redemption or repurchase of the Company's outstanding 7 1/4% zero coupon convertible subordinated notes due 2006, which the Company may be obligated to repurchase at the option of the holders thereof on April 18, 1996. Pending such uses, the net proceeds of this offering will be invested in short-term, interest-bearing securities.

CAPITALIZATION

The following table sets forth Air Group's consolidated capitalization as of March 31, 1995 and as adjusted to reflect the sale of the Debentures offered hereby, assuming no exercise of the Underwriters' over-allotment option and without giving effect to the Underwriters' discount and the payment of expenses, and does not reflect application of the net proceeds of this offering. See "Use of Proceeds."

| | MARCH 31, 1995 | |
|---|---|---|
| | ACTUAL | AS ADJUSTED |
| | (IN THOUSANDS) | |
| Indebtedness: | | |
| Short-term borrowings | $ 4,000 | $ 4,000 |
| Current portion of long-term debt and capital lease obligations | 72,080 | 72,080 |
| Notes payable due through 2009 | 325,077 | 325,077 |
| % convertible senior debentures due 2005 | -- | 100,000 |
| Convertible subordinated debentures: | | |
| 7 3/4% due 2005-2010 | 14,354 | 14,354 |
| 6 7/8% due 2000-2014 | 54,041 | 54,041 |
| 7 1/4% zero coupon convertible subordinated notes due 2006 | 130,085 | 130,085 |
| Long-term capital lease obligations | 55,679 | 55,679 |
| Total indebtedness | $ 655,316 | $ 755,316 |
| Shareholders' Equity: | | |
| Common stock, par value $1.00 per share (30,000,000 shares authorized; 13,402,186 shares outstanding) | $ 97,534 | $ 97,534 |
| Deferred compensation | (4,353) | (4,353) |
| Retained earnings | 82,132 | 82,132 |
| Total shareholders' equity | $ 175,313 | $ 175,313 |
| Total capitalization | $ 830,629 | $ 930,629 |

## RECENT OPERATING RESULTS AND DEVELOPMENTS

Air Group incurred a first quarter 1995 net loss of $16.3 million, or $1.22 per share, compared to a net loss of $6.3 million, or $0.47 per share, in the prior year's first quarter. The operating loss for the quarter was $18.3 million compared to $2.9 million for the same quarter the prior year. The 1995 results reflect lower average fares and load factors at both Alaska Airlines and Horizon.

Alaska Airlines' passenger revenues, which accounted for 86% of its total operating revenues, increased 1.5% in the first quarter of 1995 on a 17% increase in passenger traffic. Capacity increased 25% primarily due to increased flights in the Pacific Northwest-to-California market. The load factor dropped from 60.2% in the first quarter of 1994 to 56.4% in the first quarter of 1995. Passenger yields declined 13% to 11.2 cents per passenger mile in the first quarter of 1995, reflecting increased competition in the West Coast routes. Operating cost per ASM decreased 13% to 7.8 cents in the first quarter of 1995, compared to 8.9 cents in the first quarter of 1994.



During the fourth quarter of 1994 and the first quarter of 1995, Alaska Airlines experienced yield declines resulting from low fare offerings across its system. Although several fare increases have occurred since early February, the lingering effect of these low fare offerings will have an impact on second quarter results. In addition, for the past several months industry capacity increases in Alaska Airlines' West Coast markets have exceeded traffic increases, resulting in lower load factors.

MarkAir, a significant competitor of Alaska Airlines in the state of Alaska since 1992, filed for Chapter 11 bankruptcy for the second time on April 14, 1995 and ceased operating in all of Alaska Airlines' markets at the end of April 1995.

Horizon's passenger revenues, which accounted for 95% of its total operating revenues, increased 16% in the first quarter of 1995 on a 30% increase in passenger traffic. Capacity increased 34% due to the addition of larger-capacity

Fokker F-28 jets and Dornier 328 turboprop aircraft. The load factor dropped from 59.4% in the first quarter of 1994 to 57.7% in the first quarter of 1995. Passenger yields declined 11% to 31.9 cents per passenger mile in 1995, reflecting increased competition and longer passenger trips.

The International Association of Machinists (the "IAM") represents Alaska Airlines' clerical, office and passenger service employees. On April 17, 1995, Alaska Airlines and the IAM reached agreement on an amended four-year contract for these employees; the contract was ratified by the employees in early May. In April 1995, Horizon's mechanics and related classifications of the Transport Workers Union of America ratified a new three-year contract.

## PRICE RANGE OF COMMON STOCK

The Company's Common Stock is listed on the New York Stock Exchange. The following table indicates the high and low sales prices of the Common Stock as reported by the New York Stock Exchange for the periods indicated.

| | HIGH | LOW |
|---|---|---|
| 1993 | | |
| First Quarter........................ | $18 | $15 5/8 |
| Second Quarter....................... | 17 7/8 | 14 1/4 |
| Third Quarter........................ | 15 | 12 1/4 |
| Fourth Quarter....................... | 17 3/8 | 12 1/2 |
| 1994 | | |
| First Quarter........................ | $18 7/8 | $13 5/8 |
| Second Quarter....................... | 16 1/8 | 13 3/4 |
| Third Quarter........................ | 17 7/8 | 14 3/8 |
| Fourth Quarter....................... | 18 | 13 1/8 |
| 1995 | | |
| First Quarter........................ | $16 3/4 | $13 1/2 |
| Second Quarter (through June 6, 1995)............................... | 17 1/4 | 14 1/2 |



## SELECTED FINANCIAL AND OPERATING DATA

The following table summarizes selected financial and operating information for Air Group and its principal subsidiaries, Alaska Airlines and Horizon. The consolidated financial data for each of the five years ended December 31, 1994, set forth below, have been taken from the financial data included in Air Group's Form 10-K for the year ended December 31, 1994 incorporated by reference in this Prospectus Supplement and the related Registration Statement. The financial statements for the five years ended December 31, 1994 have been examined by Arthur Andersen LLP, independent public accountants. This summary should be read in conjunction with the financial statements, including the notes thereto, and other information contained in the documents incorporated by reference. The selected financial information for the three month periods ended March 31, 1995 and 1994 is unaudited but includes all adjustments (consisting only of normal recurring adjustments) that are necessary, in the opinion of management, for a fair presentation of results of operations for such periods. The airline business is seasonal in nature and the operating results for the three months ended March 31, 1995 are not necessarily indicative of results to be expected for the full year.

| | THREE MONTHS ENDED MARCH 31, | |
|---|---|---|
| | 1995 | 1994 |
| | (DOLLARS IN THOUSANDS) | |

| | | |
|---|---|---|
| CONSOLIDATED FINANCIAL DATA: | | |
| STATEMENT OF OPERATIONS DATA: | | |
| Operating revenues................ | $ 294,573 | $ 280,382 |
| Operating expenses................ | 312,874 | 283,310 |
| Operating income (loss)........... | (18,301) | (2,928) |
| Other nonoperating expense, net (a).............................. | (11,636) | (8,084) |
| Income (loss) before income tax expense and accounting change.... | (29,937) | (11,012) |
| Net income (loss)................. | $ (16,340) | $ (6,313) |
| Average primary shares outstanding (000)............................ | 13,400 | 13,349 |
| Primary earnings (loss) per share (b).............................. | $ (1.22) | $ (0.47) |
| Fully diluted earnings per share............................ | (c) | (c) |
| Cash dividends per share.......... | -- | -- |
| BALANCE SHEET DATA (AT END OF PERIOD): | | |
| Total assets...................... | $1,287,833 | $1,191,587 |
| Long-term debt and capital lease obligations...................... | 579,236 | 593,405 |
| Redeemable preferred stock........ | -- | -- |
| Shareholders' equity.............. | 175,313 | 160,919 |
| Ratio of earnings to fixed charges.......................... | (d) | (d) |
| ALASKA AIRLINES OPERATING DATA: | | |
| Revenue passenger miles (000,000)........................ | 1,793 | 1,536 |
| Available seat miles (000,000).... | 3,182 | 2,553 |
| Revenue passenger load factor..... | 56.4% | 60.2% |
| Yield per passenger mile.......... | 11.2 CENTS | 12.8 CENTS |
| Operating expenses per available seat mile........................ | 7.8 CENTS | 8.9 CENTS |
| HORIZON AIR OPERATING DATA: | | |
| Revenue passenger miles (000,000)........................ | 186 | 143 |
| Available seat miles (000,000).... | 323 | 241 |
| Revenue passenger load factor..... | 57.7% | 59.4% |
| Yield per passenger mile.......... | 31.9 CENTS | 35.7 CENTS |
| Operating expenses per available seat mile........................ | 20.6 CENTS | 22.9 CENTS |

| | YEAR ENDED DECEMBER 31, | | | | |
|---|---|---|---|---|---|
| | 1994 | 1993 | 1992 | 1991 | 1990 |
| CONSOLIDATED FINANCIAL DATA: | | | | | |
| STATEMENT OF OPERATIONS DATA: | | | | | |
| Operating revenues................ | $1,315,620 | $1,128,329 | $1,115,378 | $1,104,031 | $1,046,965 |
| Operating expenses................ | 1,240,622 | 1,145,102 | 1,210,219 | 1,069,405 | 1,018,546 |
| Operating income (loss)........... | 74,998 | (16,773) | (94,841) | 34,626 | 28,419 |
| Other nonoperating expense, net (a).............................. | (34,037) | (29,039) | (30,865) | (18,419) | (501) |
| Income (loss) before income tax expense and accounting change.... | 40,961 | (45,812) | (125,706) | 16,207 | 27,918 |
| Net income (loss)................. | $ 22,531 | $ (30,918) | $ (84,837) | $ 10,338 | $ 17,167 |
| Average primary shares outstanding (000)............................ | 13,378 | 13,340 | 13,309 | 13,413 | 13,675 |
| Primary earnings (loss) per share (b).............................. | $ 1.68 | $ (2.51) | $ (6.87) | $ 0.27 | $ 0.82 |
| Fully diluted earnings per share............................ | 1.62 | (c) | (c) | (c) | (c) |
| Cash dividends per share.......... | -- | -- | $ 0.15 | $ 0.20 | $ 0.20 |
| BALANCE SHEET DATA (AT END OF PERIOD): | | | | | |
| Total assets...................... | $1,315,771 | $1,134,954 | $1,208,358 | $1,225,455 | $1,021,404 |
| Long-term debt and capital lease obligations...................... | 589,904 | 525,418 | 487,847 | 499,971 | 281,759 |
| Redeemable preferred stock........ | -- | -- | 61,235 | 60,947 | 60,665 |
| Shareholders' equity.............. | 191,278 | 166,833 | 196,724 | 284,447 | 279,833 |
| Ratio of earnings to fixed charges.......................... | 1.36 | (d) | (d) | 1.10 | 1.32 |
| ALASKA AIRLINES OPERATING DATA: | | | | | |
| Revenue passenger miles (000,000)........................ | 7,587 | 5,514 | 5,537 | 4,948 | 4,494 |
| Available seat miles (000,000).... | 12,082 | 9,426 | 9,617 | 8,789 | 8,380 |
| Revenue passenger load factor..... | 62.8% | 58.5% | 57.6% | 56.3% | 53.6% |
| Yield per passenger mile.......... | 12.2 CENTS | 14.3 CENTS | 14.5 CENTS | 16.7 CENTS | 17.8 CENTS |

| | | | | | |
|---|---|---|---|---|---|
| Operating expenses per available seat mile........................ | 8.3 CENTS | 9.9 CENTS | 10.5 CENTS | 10.2 CENTS | 10.3 CENTS |
| HORIZON AIR OPERATING DATA: | | | | | |
| Revenue passenger miles (000,000)........................ | 733 | 560 | 486 | 405 | 357 |
| Available seat miles (000,000).... | 1,165 | 986 | 905 | 786 | 720 |
| Revenue passenger load factor..... | 62.9% | 56.8% | 53.7% | 51.5% | 49.6% |
| Yield per passenger mile.......... | 33.3 CENTS | 37.9 CENTS | 40.7 CENTS | 42.9 CENTS | 43.4 CENTS |
| Operating expenses per available seat mile........................ | 21.0 CENTS | 21.8 CENTS | 22.2 CENTS | 22.3 CENTS | 21.9 CENTS |

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(a) Includes capitalized interest of $0 and $.1 million for the three months ended March 31, 1995 and 1994, respectively, and $.4 million, $.5 million, $6.1 million, $8.3 million and $9.0 million for the year ended December 31, 1994, 1993, 1992, 1991 and 1990, respectively.

(b) For 1992, primary earnings per share includes $(.34) for the $4.6 million cumulative effect of the postretirement benefits accounting change as of January 1, 1992.

(c) Antidilutive.

(d) For 1993 and 1992, earnings are inadequate to cover fixed charges by $46.3 million and $131.8 million, respectively. For the three months ended March 31, 1995 and 1994, earnings are inadequate to cover fixed charges by $29.9 million and $11.1 million, respectively.



REVENUE PASSENGER MILES--THE NUMBER OF PAYING PASSENGERS ON A FLIGHT MULTIPLIED BY THE ROUTE MILES OF THAT FLIGHT, SUMMED FOR ALL PASSENGER FLIGHTS.

AVAILABLE SEAT MILES--AIRCRAFT MILES FLOWN MULTIPLIED BY THE NUMBER OF AVAILABLE SEATS ON THE AIRCRAFT; REPRESENTS THE TOTAL PASSENGER CARRYING CAPACITY OFFERED.

REVENUE PASSENGER LOAD FACTOR--REVENUE PASSENGER MILES DIVIDED BY AVAILABLE SEAT MILES; REPRESENTS THE PERCENTAGE OF AVAILABLE SEAT CAPACITY OCCUPIED BY REVENUE PASSENGERS.

YIELD PER PASSENGER MILE--REPRESENTS THE AVERAGE PASSENGER REVENUE RECEIVED FOR EACH MILE A PASSENGER IS CARRIED.

OPERATING EXPENSES PER AVAILABLE SEAT MILE--REPRESENTS THE RESULT OF OPERATING EXPENSES DIVIDED BY AVAILABLE SEAT MILES.



## DESCRIPTION OF THE DEBENTURES

The following description of the particular terms of the Debentures offered hereby (referred to in the accompanying Prospectus as the "Convertible Debt Securities") supplements and, to the extent inconsistent therewith, replaces the description of the general terms and provisions of the Convertible Debt Securities set forth in the accompanying Prospectus, to which description reference is hereby made. Capitalized terms used but not defined herein or in the accompanying Prospectus have the meanings given to them in the Indenture (as hereinafter defined) or the Supplemental Indenture (as hereinafter defined). Section references are to the Supplemental Indenture unless otherwise indicated.

### GENERAL

The Debentures will constitute senior unsecured obligations of the Company limited to $100,000,000 aggregate principal amount, plus such additional amount not in excess of $15,000,000 as may be purchased by the Underwriters upon exercise of the over-allotment option. See "Underwriting." The Debentures will mature on June 15, 2005. The Debentures will constitute a series of Convertible Senior Debt Securities (as defined in the accompanying Prospectus) and will be issued under an Indenture, dated as of June , 1995 (the "Indenture"), between the Company and Harris Trust and Savings Bank, as trustee (the "Trustee"), the terms of which are more fully described in the accompanying Prospectus, as supplemented by a Supplemental Indenture, dated as of June , 1995 (the "Supplemental Indenture"), between the Company and the Trustee. The Debentures will be issued only in fully registered form in denominations of $1,000 and integral multiples thereof. Principal, premium, if any, and interest on the Debentures will be payable at the corporate trust office of Bank of Montreal Trust Company in New York, New York.

Interest on the Debentures will accrue at the rate of % per annum and will be payable semiannually on June 15 and December 15 of each year, commencing December 15, 1995, to the holders of record of Debentures on the June 1 and December 1 next preceding such interest payment date. Interest on the Debentures will accrue from the most recent date to which interest has been paid or, if no interest has been paid, from the original date of issuance.

CONVERSION

The Debentures will be convertible at their principal amount or any portion thereof that is an integral multiple of $1,000 at any time prior to maturity, subject to prior redemption at the Company's option on or after June 15, 1998 or purchase by the Company at the holder's option in the event of any Change in Control (as hereinafter defined), into shares of Common Stock, at the conversion price set forth on the front cover page hereof, subject to adjustment as described below. The Company will not be required to issue fractional shares of Common Stock, but will pay a cash adjustment in lieu thereof. In the case of any Debenture or portion thereof called for redemption, conversion rights will expire at the close of business on the business day immediately preceding the redemption date. Interest accrued shall not be paid on converted Debentures; PROVIDED, HOWEVER, that if any Debenture is called for redemption on June 15, 1998, and such Debenture is surrendered for conversion at any time during the 10 business days immediately preceding the date fixed for redemption, interest shall accrue on such Debenture through the date fixed for redemption and shall be payable on such redemption date to the person who surrenders such Debenture for conversion. If any Debenture not called for redemption is converted between a record date for the payment of interest and the next succeeding interest payment date, such Debenture must be accompanied by funds equal to the interest payable on such interest payment date on the principal amount so converted. (Section 2.4.)

The conversion price is subject to adjustment in certain events, including (a) the subdivision, combination or reclassification of the Company's outstanding Common Stock, (b) the issuance by the Company of Common Stock as a dividend or distribution on the Common Stock, (c) the issuance of rights or warrants to all holders of Common Stock entitling them to subscribe for or purchase shares of Common Stock (or securities convertible into or exchangeable for Common Stock) at a price per share (or having a conversion or exercise price per share) less than the current market price (as defined in the Supplemental Indenture) of the Common Stock on the record date, and (d) the distribution by the Company to all holders of Common Stock of shares of capital stock other than Common Stock, debt securities or assets or rights or warrants to purchase assets or securities of the Company (excluding the rights and warrants referred to in clause (c) and



cash dividends or other cash distributions from consolidated current net earnings or earned surplus or dividends payable in Common Stock but including Extraordinary Cash Dividends). In the Supplemental Indenture, "current market price" is defined as the average of the last reported sale price of the Common Stock on the New York Stock Exchange for 30 consecutive trading days commencing 45 trading days before the date in question. There will be no upward adjustment in the conversion price except in the event of a reverse stock split. No adjustment of the conversion price will be required to be made until the cumulative adjustments require an increase or decrease of at least 1% in the conversion price as last adjusted. (Section 2.4.)

Certain adjustments to the conversion price to reflect the Company's issuance of certain rights, warrants, evidences of indebtedness, securities or other assets to holders of Common Stock may result in constructive distributions taxable as dividends to U.S. holders of the Debentures. Similarly, if instead of adjusting the conversion price upon such issuance, the Company elects at such time to alter the consideration receivable by the holders of the Debentures upon conversion to include the assets such holders would have been entitled to if conversion had occurred prior to the record date for such issuance, the alteration may result in constructive distributions taxable as dividends to U.S. holders of the Debentures.

Subject to any applicable right of the holders upon a Change in Control, in case of any reclassification (excluding those referred to above), merger, consolidation, sale or conveyance by the Company of all or substantially all of the Company's assets as an entirety, the holder of each outstanding Debenture shall have the right to convert such Debenture only into the kind and amount of shares of stock and other securities and property (including cash) receivable in such transaction by a holder of the number of shares of Common Stock into which such Debenture was convertible immediately prior to the effective date of the transaction.

REDEMPTION

The Debentures will be redeemable, in whole or in part, at the Company's option on not less than 30, nor more than 60, days' prior notice to each holder of Debentures to be redeemed, at any time on or after June 15, 1998, at the redemption prices (expressed as percentages of the principal amount) set forth below, plus accrued and unpaid interest to the redemption date, if redeemed during the 12-month period beginning June 15 of the calendar years indicated:

| YEAR | REDEMPTION PRICE |
|---|---|
| 1998.......................................... | % |
| 1999.......................................... | % |
| 2000.......................................... | % |
| 2001.......................................... | % |
| 2002.......................................... | % |
| 2003.......................................... | % |

and, on or after June 15, 2004, at 100% of principal amount. (Section 2.5.)

If less than all the Debentures are to be redeemed, the Trustee shall select the Debentures or portions thereof to be redeemed by any method the Trustee deems fair and appropriate. (Section 10.3 of the Indenture.) There is no sinking fund for the Debentures.

RANKING

The Debentures will constitute senior unsecured obligations of the Company and will rank PARI PASSU in right of payment to the Company's other senior unsecured indebtedness. As of the date hereof, the Company had no other senior unsecured indebtedness. The Company is a holding company and, accordingly, the Debentures will be effectively subordinated to all existing and future liabilities of the Company's operating subsidiaries, including Alaska Airlines and Horizon. As of March 31, 1995, the long-term debt and capital lease obligations of Alaska Airlines and of Horizon were $438.0 million and $3.6 million, respectively.

PURCHASE OF DEBENTURES UPON CHANGE IN CONTROL

In the event of any Change in Control, each holder will have the right, at the holder's option, subject to the terms and conditions of the Indenture, to require the Company to purchase all or any part (provided that



the principal amount must be $1,000 or an integral multiple thereof) of the holder's Debentures on the date that is 35 business days after the occurrence of such Change in Control (the "Change in Control Purchase Date") at a cash purchase price (the "Change in Control Purchase Price") equal to 100% of the principal amount thereof plus accrued and unpaid interest, if any, to the Change in Control Purchase Date. (Section 2.6.)

Within 15 business days after the Change in Control, the Company shall mail to the Trustee, who shall mail to each holder (and to beneficial owners as required by applicable law), a notice regarding the Change in Control, which notice shall state, among other things: (a) the date of such Change in Control and, briefly, the events causing such Change in Control, (b) the last date on which the Change in Control Purchase Notice (as hereinafter defined) must be given, (c) the Change in Control Purchase Date, (d) the Change in Control Purchase Price, (e) the name and address of the Paying Agent and the Conversion Agent, (f) the conversion rate and any adjustments thereto, (g) that Debentures with respect to which a Change in Control Purchase Notice is given by the holder may be converted into shares of Common Stock only if the Change in Control Purchase Notice has been withdrawn in accordance with the terms of the Indenture, (h) the procedures that holders must follow to exercise these rights, (i) the procedure for withdrawing a Change in Control Purchase Notice, (j) that holders who want to convert Debentures must satisfy the procedural requirements set forth in paragraph 3 of the Debentures, and (k) briefly, the conversion rights of holders of the Debentures. (Section 2.6.)

To exercise the purchase right, the holder must deliver written notice of the exercise of such right (a "Change in Control Purchase Notice") to the Paying Agent or an office or agency maintained by the Company for such purpose in the Borough of Manhattan, The City of New York, New York prior to the close of business on the Change in Control Purchase Date. (Section 2.6.) The Change in Control Purchase Notice shall state (a) the certificate numbers of the Debentures to be delivered by the holder thereof for purchase by the Company; (b) the portion of the principal amount of Debentures to be purchased, which portion must be $1,000 or an integral multiple thereof; and (c) that such Debentures are to be purchased by the Company pursuant to the applicable provisions of the Debentures. (Section 2.6.)

Any Change in Control Purchase Notice may be withdrawn by the holder by a written notice of withdrawal delivered to the Paying Agent or to any other office or agency mandated by the Company for such purpose prior to the close of business on the Change in Control Purchase Date. The notice of withdrawal shall state the principal amount and the certificate numbers of the Debentures as to which the withdrawal notice relates and the principal amount, if any, that remains subject to a Change in Control Purchase Notice. (Section 2.6.)

Payment of the Change in Control Purchase Price for a Debenture for which a Change in Control Purchase Notice has been delivered and not withdrawn is conditioned on delivery of such Debenture (together with the necessary endorsements) to the Paying Agent or an office or agency maintained by the Company for such purpose in the Borough of Manhattan, The City of New York, New York at any time (whether prior to, on or after the Change in Control Purchase Date) after the delivery of such Change in Control Purchase Notice. Payment of the Change in Control Purchase Price for such Debenture will be made promptly following the later of the Change in Control Purchase Date and the time of delivery of such Debenture. If the Paying Agent holds, in accordance with the terms of the Supplemental Indenture, money sufficient to pay the Change in Control Purchase Price of such Debenture on the business day following the Change in Control Purchase Date, then, on and after the Change in Control Purchase Date, such Debenture will cease to be outstanding and interest on such Debenture will cease to accrue and will be deemed paid, whether or not such Debenture is delivered to the Paying Agent, and all other rights of the holder shall terminate (other than the right to receive the Change in Control Purchase Price upon delivery of such Debenture). (Section 2.6.)

Under the Supplemental Indenture, a "Change in Control" of the Company is deemed to have occurred at such time as (a) any "person" or "group" (within the meaning of Section 13(d)(3) or 14(d)(2) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) other than the Company, any subsidiary of the Company or any employee benefit plan or stock ownership plan of either the Company or any subsidiary of the Company, (i) files a Schedule 13D or 14D-1 under the Exchange Act (or any successor schedule, form or report) disclosing that such person has become the "beneficial owner" of 50% or more of the Company's capital stock having the power to vote in the election of directors under ordinary circumstances ("Voting Stock"), with certain exceptions, (ii) acquires more than 50% of the Company's assets, or (iii) acquires more than 50% of the assets or Voting Stock of any subsidiary (A) the total assets of which exceed 50% of the consolidated total assets of the Company and its subsidiaries or (B) the operating income of which exceeded 50% of the average of the consolidated operating income of the Company and its subsidiaries for the Company's three most recently completed fiscal years, or (b) there shall be consummated any consolidation or merger of the Company (i) in which the Company is not the resulting or surviving corporation or (ii) pursuant to which any Voting Stock of the Company would be converted into cash, securities or other property, in each case other than a consolidation or merger of the Company in which the holders of such Voting Stock immediately prior to the consolidation or merger have at least a majority of the Voting Stock, directly or indirectly, of the resulting or surviving corporation immediately after the consolidation or merger. (Section 1.2.) The Supplemental Indenture does not permit the Company's Board of Directors to waive the Company's obligation to purchase Debentures at a holder's option in the event of a Change in Control of the Company. (Section 2.6.)

The Company shall comply with the provisions of Rule 13e-4 and any other tender offer rules under the Exchange Act that may then be applicable, and will file a Schedule 13E-4 or any other schedule required thereunder in connection with any offer by the Company to purchase Debentures at the option of the holders thereof upon a Change in Control. (Section 2.6.) The Change in Control purchase feature of the Debentures may in certain circumstances make more difficult or discourage a takeover of the Company and, thus, the removal of incumbent management.

If a Change in Control Offer is made, there can be no assurance that the Company would have funds sufficient to pay the Change in Control Purchase Price for all the Debentures that might be delivered by holders of Debentures seeking to exercise the purchase right. In addition, the Company's ability to purchase Debentures with cash may be limited by the terms of its then existing borrowing arrangements. The Company's ability to purchase Debentures with cash may also be limited by the terms of its subsidiaries' then existing debt agreements due to dividend restrictions, since the Company's source of funds for any such purchase will be primarily from dividends and other payments from its subsidiaries. No Debentures may be purchased pursuant to the provisions described above if there has occurred and is continuing an Event of Default described under "--Certain Covenants and Events of Default" in this Prospectus Supplement (other than a default in the payment of the Change in Control Purchase Price with respect to such Debentures).

Notwithstanding the foregoing, the provisions described above with respect to a Change in Control will not prevent a takeover or recapitalization of the Company that would otherwise comply with the provisions described under "Description of Convertible Debt Securities--Consolidation, Merger or Sale by the Issuer" in the accompanying Prospectus.

## DEFEASANCE

The provisions described under "Description of Convertible Debt Securities--Covenant Defeasance" in the accompanying Prospectus are not applicable to the Debentures.

## CERTAIN COVENANTS AND EVENTS OF DEFAULT

The provisions of the Indenture that are described in the accompanying Prospectus under "Description of Convertible Debt Securities--General," "--Consolidation, Merger or Sale by the Issuer," "--Events of Default, Notice and Certain Rights on Default" and "--Payment, Registration, Transfer and Exchange" will apply to the Debentures. The provisions of the Indenture that are described in the accompanying Prospectus under "Description of Convertible Debt Securities--Modification of the Indentures" will also apply to the Debentures; PROVIDED, HOWEVER, that no modification or amendment of the Indenture may, without the consent of the holder of each outstanding Debenture affected thereby, make any change (a) to the definition of the term "Change in Control" or (b) that adversely affects the right to convert, or the conversion price for, any Debenture.



THE TRUSTEE

Harris Trust and Savings Bank will be the Trustee under the Indenture for the Debentures. An affiliate of Harris Trust and Savings Bank serves as trustee with respect to the Company's 7 3/4% Convertible Subordinated Debentures due 2005-2010 and the Company's 7 1/4% zero coupon convertible subordinated notes due 2006.



UNDERWRITING

Subject to the terms and conditions set forth in a purchase agreement (the "Purchase Agreement") between the Company and the several underwriters listed below (the "Underwriters"), the Company has agreed to sell to the Underwriters, and the Underwriters have severally agreed to purchase from the Company, the respective principal amounts of the Debentures set forth opposite their names below. The Purchase Agreement provides that the obligations of the Underwriters are subject to certain conditions precedent and that the Underwriters will be obligated to purchase all the Debentures if any are purchased.

| UNDERWRITER | PRINCIPAL AMOUNT |
| --- | --- |
| Merrill Lynch, Pierce, Fenner & Smith Incorporated | $ |
| Goldman, Sachs & Co. | |
| Total | $ 100,000,000 |

The Underwriters have advised the Company that they propose initially to offer the Debentures to the public at the public offering price set forth on the cover page of this Prospectus Supplement, and to certain dealers at such price less a concession not in excess of % of the principal amount of the Debentures. The Underwriters may allow, and such dealers may reallow, a discount not in excess of % of the principal amount of the Debentures to certain other dealers. After the initial public offering, the public offering price, concession and discount may be changed.

The Company has granted the Underwriters an option, exercisable for 30 days after the date of this Prospectus Supplement, to purchase up to an additional $15,000,000 principal amount of Debentures to cover over-allotments, if any, at the initial public offering price less the underwriting discount.

The Company has been advised by the Underwriters that the Underwriters presently intend to make a market in the Debentures offered hereby; however, they are not obligated to do so. Any market making may be discontinued at any time, and there can be no assurance that an active public market for the Debentures will develop.

The Company has agreed not to sell to any person other than the Underwriters any shares of Common Stock or securities convertible into or exchangeable or exercisable for Common Stock (other than (a) shares issuable upon conversion of the Debentures, (b) shares issuable upon the exercise or conversion of currently outstanding securities of the Company and (c) the grant of certain rights pursuant to employee benefit plans) without the prior written consent of Merrill Lynch, Pierce, Fenner & Smith Incorporated, on behalf of the Underwriters, for a period of 90 days after the date of this Prospectus Supplement.

The Company has agreed to indemnify the several Underwriters against certain liabilities, including civil liabilities under the Securities Act of 1933, as amended.

The Underwriters, from time to time, perform investment banking and other financial services for the Company and its subsidiaries, including Alaska Airlines and Horizon.

## LEGAL OPINIONS

The validity of the Debentures offered hereby will be passed upon for Air Group by Perkins Coie, Seattle, Washington, and for the Underwriters by Shearman & Sterling, New York, New York.

## EXPERTS

The consolidated financial statements and schedule of Air Group at December 31, 1994 and for each of the three years in the period ended December 31, 1994, incorporated by reference in this Prospectus Supplement and the related Registration Statement, have been audited by Arthur Andersen LLP, independent public accountants, as indicated in their reports with respect thereto, and are incorporated herein and therein in reliance upon the authority of said firm as experts in accounting and auditing in giving said reports.