
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 8-K

CURRENT REPORT PURSUANT
TO SECTION 13 OR 15(D) OF THE
SECURITIES EXCHANGE ACT OF 1934

July 26, 2018
(Date of earliest event reported)

ALASKA AIR GROUP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of Incorporation)

1-8957
(Commission File Number)

91-1292054
(IRS Employer Identification No.)

19300 International Boulevard, Seattle, Washington
(Address of Principal Executive Offices)

98188
(Zip Code)

(206) 392-5040
(Registrant's Telephone Number, Including Area Code)

(Former Name or Former Address, if Changed Since Last Report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (*see* General Instruction A.2. below):

- ☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
- ☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
- ☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
- ☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Indicate by check mark whether the registrant is an emerging growth company as defined in Rule 405 of the Securities Act of 1933 (17 CFR 230.405) or Rule 12b-2 of the Securities Exchange Act of 1934 (17 CFR 240.12b-2).

☐ Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

ITEM 2.02. Results of Operations And Financial Condition

On July 26, 2018, Alaska Air Group, Inc. (Air Group) issued a press release reporting financial results for the second quarter of 2018. The press release is furnished herein as Exhibit 99.1.

ITEM 7.01. Regulation FD Disclosure

Pursuant to 17 CFR Part 243 (Regulation FD), the Company is submitting information relating to its financial and operational outlook in an Investor Update as attached in Exhibit 99.2.

In accordance with General Instruction B.2 of Form 8-K, the information under this item and Exhibit 99.2 shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the Exchange Act), nor shall such information be deemed incorporated by reference in any filing under the Securities Act of 1933, as amended, except as shall be expressly set forth by specific reference in such a filing. This report will not be deemed an admission as to the materiality of any information required to be disclosed solely to satisfy the requirements of Regulation FD.

ITEM 9.01 Financial Statements and Other Exhibits

[Exhibit 99.1](#) Second Quarter 2018 Earnings Press Release dated July 26, 2018

[Exhibit 99.2](#) Investor Update dated July 26, 2018

Signatures

Pursuant to the requirements 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.

Registrant

Date: July 26, 2018

/s/ Brandon S. Pedersen

Brandon S. Pedersen

Executive Vice President/Finance and Chief Financial Officer

Alaska Air Group

July 26, 2018

Media contact:

Media Relations
(206) 304-0008

Investor/analyst contact:

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Director, Investor Relations
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Alaska Air Group Reports Second Quarter 2018 Results

Financial Highlights:

- Reported net income for the second quarter under Generally Accepted Accounting Principles (GAAP) of \$193 million, or \$1.56 per diluted share, compared to net income of \$293 million, or \$2.36 per diluted share in the second quarter of 2017. As the company has recently implemented new accounting standards, including the standards relating to revenue recognition and retirement benefits, 2017 financial information has been adjusted.
- Reported second quarter 2018 adjusted diluted earnings per share of \$1.66 compared to \$2.48 reported in the second quarter of 2017. Second quarter adjusted net income excluding special items such as merger-related costs and mark-to-market fuel hedge accounting adjustments was \$206 million compared to \$309 million in the second quarter of 2017. This quarter's adjusted results compare to the First Call analyst consensus estimate of \$1.63 per share.
- Paid a \$0.32 per-share quarterly cash dividend in the second quarter, a 7% increase over the dividend paid in the second quarter of 2017.
- Repurchased a total of 389,739 shares of common stock for approximately \$25 million in the first six months of 2018.
- Generated approximately \$725 million of operating cash flow, including merger-related costs and other special items.
- Held \$1.6 billion in unrestricted cash and marketable securities as of June 30, 2018.

Operational Highlights:

- Transitioned to a single Passenger Service System (PSS) in April 2018, enabling us to provide one reservation system, one website and one inventory of flights to our guests.
- Reached a merger transition agreement with the Transport Workers Union (TWU) to combine Boeing and Airbus dispatchers into a single group.
- Completed Premium Class rollout on our Boeing 737-800, 900 and 900ER fleets.
- Added Aer Lingus as a global Mileage Plan partner.
- Added two Boeing 737-900ER aircraft and two Airbus A321neo aircraft to the mainline operating fleet in the second quarter of 2018. Added four Embraer 175 (E175) regional jets to Horizon Air's fleet in the second quarter of 2018 and four E175 aircraft operated by SkyWest Airlines.

Recognition and Awards:

- Ranked "Highest in Customer Satisfaction Among Traditional Carriers" in 2018 by J.D. Power for the 11th year in a row.
- Received top honors in three Skytrax World Airline Awards categories including "Best Regional Airline in North America," "Best Airline Staff in North America," and "Best Cabin Crew in the USA."
- Virgin America was rated Best Domestic Airline in Travel + Leisure "World's Best Awards" for 11 years in a row.
- Ranked among Forbes' 2018 "America's Best Employers" for the fourth year in a row.
- Awarded "Best Food and Beverage in the Americas" by Airline Passenger Service Experience Association (APEX) passenger choice awards for 2018.
- Received 17th Diamond Award of Excellence from the Federal Aviation Administration, recognizing both Alaska and Horizon's aircraft technicians for their commitment to training.

SEATTLE — Alaska Air Group, Inc., (NYSE: ALK) today reported second quarter 2018 GAAP net income of \$193 million, or \$1.56 per diluted share, compared to \$293 million, or \$2.36 per diluted share in the second quarter of 2017. Excluding the impact of merger-related costs and mark-to-market fuel hedge adjustments, the company reported adjusted net income of \$206 million, or \$1.66 per diluted share, compared to \$309 million, or \$2.48 per diluted share, in 2017.

"In the last year and half, we've made tremendous progress bringing Alaska Airlines and Virgin America together," said CEO Brad Tilden. "We're on very solid footing today thanks to the fantastic efforts of our employees, who delivered exceptional on-time performance and earned our 11th consecutive J.D. Power award for highest in customer satisfaction - all while completing the most complex part of our integration."

The following table reconciles the company's reported GAAP net income and earnings per diluted share (diluted EPS) for the three and six months ended June 30, 2018 and 2017 to adjusted amounts.

| <i>(in millions, except per-share amounts)</i> | Three Months Ended June 30, | | | |
|--|-----------------------------|----------------|---------------------|----------------|
| | 2018 | | 2017 ^(a) | |
| | Dollars | Diluted EPS | Dollars | Diluted EPS |
| GAAP net income and diluted EPS | \$ 193 | \$ 1.56 | \$ 293 | \$ 2.36 |
| Mark-to-market fuel hedge adjustments | (22) | (0.18) | 2 | 0.02 |
| Special items—merger-related costs | 39 | 0.31 | 24 | 0.19 |
| Income tax effect | (4) | (0.03) | (10) | (0.09) |
| Non-GAAP adjusted net income and diluted EPS | <u>\$ 206</u> | <u>\$ 1.66</u> | <u>\$ 309</u> | <u>\$ 2.48</u> |

| <i>(in millions, except per-share amounts)</i> | Six Months Ended June 30, | | | |
|--|---------------------------|----------------|---------------------|----------------|
| | 2018 | | 2017 ^(a) | |
| | Dollars | Diluted EPS | Dollars | Diluted EPS |
| GAAP net income and diluted EPS | \$ 197 | \$ 1.59 | \$ 386 | \$ 3.10 |
| Mark-to-market fuel hedge adjustments | (35) | (0.28) | 12 | 0.10 |
| Special items—employee tax reform bonus | 25 | 0.20 | — | — |
| Special items—merger-related costs | 45 | 0.36 | 63 | 0.51 |
| Income tax effect | (8) | (0.06) | (28) | (0.23) |
| Non-GAAP adjusted net income and diluted EPS | <u>\$ 224</u> | <u>\$ 1.81</u> | <u>\$ 433</u> | <u>\$ 3.48</u> |

(a) Certain historical information has been adjusted to reflect the adoption of new accounting standards.

Statistical data, as well as a reconciliation of the reported non-GAAP financial measures, can be found in the accompanying tables. A glossary of financial terms can be found on the last page of this release.

A conference call regarding the second quarter results will be streamed online at 8:30 a.m. Pacific time on July 26, 2018. It can be accessed at www.alaskaair.com/investors. For those unable to listen to the live broadcast, a replay will be available after the conclusion of the call.

References in this news release to "Air Group," "company," "we," "us" and "our" refer to Alaska Air Group, Inc. and its subsidiaries, unless otherwise specified. Alaska Airlines, Inc., Horizon Air Industries, Inc., and Virgin America Inc. are referred to as "Alaska," "Horizon," and "Virgin America" respectively, and together as our "airlines."

This news release may contain forward-looking statements subject to the safe harbor protection provided by Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995. These statements relate to future events and involve known and unknown risks and uncertainties that may cause actual outcomes to be materially different from those indicated by any forward-looking statements. For a comprehensive discussion of potential risk factors, see Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2017, as well as in other documents filed by the Company with the SEC after the date thereof. Some of these risks include general economic conditions, increases in operating costs including fuel, competition, labor costs and relations, our indebtedness, inability to meet cost reduction goals, seasonal fluctuations in our financial results, an aircraft accident, changes in laws and regulations and risks inherent in the achievement of anticipated synergies and the timing thereof in connection with the acquisition of Virgin America. All of the forward-looking statements are qualified in their entirety by reference to the risk factors discussed therein. We operate in a continually changing business environment, and new risk factors emerge from time to time. Management cannot predict such new risk factors, nor can it assess the impact, if any, of such new risk factors on our business or events described in any forward-looking statements. We expressly disclaim any obligation to publicly update or revise any forward-looking statements after the date of this report to conform them to actual results. Over time, our actual results, performance or achievements will likely differ from the anticipated results, performance, or achievements that are expressed or implied by our forward-looking statements, and such differences might be significant and materially adverse.

Alaska Airlines and its regional partners fly 44 million guests a year to more than 115 destinations with an average of 1,200 daily flights across the United States and to Mexico, Canada and Costa Rica. With Alaska and [Alaska Global Partners](#), guests can earn and redeem miles on flights to more than 900 destinations worldwide. Alaska Airlines ranked "Highest in Customer Satisfaction Among Traditional Carriers in North America" in the J.D. Power North America Airline Satisfaction Study for 11 consecutive years from 2008 to 2018. Learn about Alaska's award-winning service at newsroom.alaskaair.com and blog.alaskaair.com. Alaska Airlines and Horizon Air are subsidiaries of Alaska Air Group (NYSE: ALK).

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

Alaska Air Group, Inc.

| <i>(in millions, except per-share amounts)</i> | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|---|-----------------------------|---------------------|--------------|---------------------------|---------------------|--------------|
| | 2018 | 2017 ^(a) | Change | 2018 | 2017 ^(a) | Change |
| Operating Revenues: | | | | | | |
| Passenger revenue | \$ 1,997 | \$ 1,945 | 3 % | \$ 3,682 | \$ 3,547 | 4 % |
| Mileage plan other revenue | 108 | 109 | (1)% | 215 | 209 | 3 % |
| Cargo and other | 51 | 48 | 6 % | 91 | 86 | 6 % |
| Total Operating Revenues | 2,156 | 2,102 | 3 % | 3,988 | 3,842 | 4 % |
| Operating Expenses: | | | | | | |
| Wages and benefits | 544 | 470 | 16 % | 1,080 | 920 | 17 % |
| Variable incentive pay | 38 | 27 | 41 % | 77 | 58 | 33 % |
| Aircraft fuel, including hedging gains and losses | 475 | 344 | 38 % | 884 | 683 | 29 % |
| Aircraft maintenance | 106 | 96 | 10 % | 213 | 183 | 16 % |
| Aircraft rent | 77 | 69 | 12 % | 151 | 134 | 13 % |
| Landing fees and other rentals | 110 | 99 | 11 % | 236 | 214 | 10 % |
| Contracted services | 76 | 77 | (1)% | 157 | 158 | (1)% |
| Selling expenses | 88 | 102 | (14)% | 166 | 185 | (10)% |
| Depreciation and amortization | 97 | 90 | 8 % | 191 | 180 | 6 % |
| Food and beverage service | 55 | 50 | 10 % | 105 | 95 | 11 % |
| Third-party regional carrier expense | 39 | 27 | 44 % | 76 | 54 | 41 % |
| Other | 141 | 140 | 1 % | 282 | 271 | 4 % |
| Special items—merger-related costs | 39 | 24 | 63 % | 45 | 63 | (29)% |
| Special items—other | — | — | — % | 25 | — | NM |
| Total Operating Expenses | 1,885 | 1,615 | 17 % | 3,688 | 3,198 | 15 % |
| Operating Income | 271 | 487 | (44)% | 300 | 644 | (53)% |
| Nonoperating Income (Expense): | | | | | | |
| Interest income | 10 | 9 | | 18 | 16 | |
| Interest expense | (25) | (26) | | (49) | (51) | |
| Interest capitalized | 4 | 4 | | 9 | 8 | |
| Other—net | (1) | — | | (13) | (1) | |
| Total Nonoperating Income (Expense) | (12) | (13) | | (35) | (28) | |
| Income (Loss) Before Income Tax | 259 | 474 | | 265 | 616 | |
| Income tax expense | 66 | 181 | | 68 | 230 | |
| Net Income (Loss) | \$ 193 | \$ 293 | | \$ 197 | \$ 386 | |
| Basic Earnings (Loss) Per Share: | | | | | | |
| | \$ 1.57 | \$ 2.37 | | \$ 1.60 | \$ 3.12 | |
| Diluted Earnings (Loss) Per Share: | | | | | | |
| | \$ 1.56 | \$ 2.36 | | \$ 1.59 | \$ 3.10 | |
| Shares Used for Computation: | | | | | | |
| Basic | 123.268 | 123.573 | | 123.212 | 123.534 | |
| Diluted | 124.036 | 124.332 | | 123.953 | 124.374 | |
| Cash dividend declared per share: | | | | | | |
| | \$ 0.320 | \$ 0.300 | | \$ 0.640 | \$ 0.600 | |

(a) Certain historical information has been adjusted to reflect the adoption of new accounting standards.

CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)

Alaska Air Group, Inc.

| <i>(in millions)</i> | June 30, 2018 | December 31, 2017 ^(a) |
|---|------------------|----------------------------------|
| Cash and marketable securities | \$ 1,568 | \$ 1,621 |
| Total current assets | 2,216 | 2,152 |
| Property and equipment—net | 6,493 | 6,284 |
| Goodwill | 1,943 | 1,943 |
| Intangible assets | 130 | 133 |
| Other assets | 273 | 234 |
| Total assets | 11,055 | 10,746 |
| Air traffic liability | 1,112 | 806 |
| Current portion of long-term debt | 314 | 307 |
| Other current liabilities | 1,610 | 1,573 |
| Current liabilities | 3,036 | 2,686 |
| Long-term debt | 1,998 | 2,262 |
| Other liabilities and credits | 2,428 | 2,338 |
| Shareholders' equity | 3,593 | 3,460 |
| Total liabilities and shareholders' equity | \$ 11,055 | \$ 10,746 |
| Debt-to-capitalization ratio, adjusted for aircraft operating leases ^(b) | 52% | 53% |
| Number of common shares outstanding | 123.204 | 123.061 |

(a) Certain historical information has been adjusted to reflect the adoption of new accounting standards.

(b) Calculated using the present value of remaining aircraft lease payments.

OPERATING STATISTICS SUMMARY (unaudited)
Alaska Air Group, Inc.

| | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|---|-----------------------------|--------|-----------|---------------------------|--------|-----------|
| | 2018 | 2017 | Change | 2018 | 2017 | Change |
| Consolidated Operating Statistics:^(a) | | | | | | |
| Revenue passengers (000) | 12,069 | 11,391 | 6.0% | 22,558 | 21,399 | 5.4% |
| RPMs (000,000) "traffic" | 14,484 | 13,554 | 6.9% | 26,887 | 25,262 | 6.4% |
| ASMs (000,000) "capacity" | 16,833 | 15,612 | 7.8% | 32,313 | 30,006 | 7.7% |
| Load factor | 86.0% | 86.8% | (0.8) pts | 83.2% | 84.2% | (1.0) pts |
| Yield ^(d) | 13.79¢ | 14.36¢ | (4.0)% | 13.69¢ | 14.04¢ | (2.5)% |
| RASM ^(d) | 12.81¢ | 13.46¢ | (4.8)% | 12.34¢ | 12.80¢ | (3.6)% |
| CASMex ^{(b)(d)} | 8.14¢ | 7.98¢ | 2.0% | 8.46¢ | 8.17¢ | 3.5% |
| Economic fuel cost per gallon ^(b) | \$2.30 | \$1.71 | 34.5% | \$2.22 | \$1.75 | 26.9% |
| Fuel gallons (000,000) | 216 | 201 | 7.5% | 413 | 385 | 7.3% |
| ASM's per gallon | 77.9 | 77.7 | 0.3% | 78.2 | 77.9 | 0.4% |
| Average number of full-time equivalent employees (FTE) | 21,655 | 19,745 | 9.7% | 21,461 | 19,214 | 11.7% |
| Mainline Operating Statistics: | | | | | | |
| Revenue passengers (000) | 9,462 | 8,941 | 5.8% | 17,673 | 16,715 | 5.7% |
| RPMs (000,000) "traffic" | 13,221 | 12,525 | 5.6% | 24,581 | 23,352 | 5.3% |
| ASMs (000,000) "capacity" | 15,289 | 14,341 | 6.6% | 29,387 | 27,602 | 6.5% |
| Load factor | 86.5% | 87.3% | (0.8) pts | 83.6% | 84.6% | (1.0) pts |
| Yield ^(d) | 12.95¢ | 13.40¢ | (3.4)% | 12.83¢ | 13.07¢ | (1.8)% |
| RASM ^(d) | 12.16¢ | 12.77¢ | (4.8)% | 11.70¢ | 12.11¢ | (3.4)% |
| CASMex ^{(b)(d)} | 7.43¢ | 7.18¢ | 3.5% | 7.71¢ | 7.35¢ | 4.9% |
| Economic fuel cost per gallon ^(b) | \$2.29 | \$1.70 | 34.7% | \$2.22 | \$1.74 | 27.6% |
| Fuel gallons (000,000) | 188 | 179 | 5.0% | 360 | 343 | 5.0% |
| ASM's per gallon | 81.3 | 80.3 | 1.2% | 81.5 | 80.5 | 1.2% |
| Average number of FTE's | 16,477 | 15,447 | 6.7% | 16,245 | 15,227 | 6.7% |
| Aircraft utilization | 11.6 | 11.4 | 1.8% | 11.4 | 11.1 | 2.7% |
| Average aircraft stage length | 1,298 | 1,294 | 0.3% | 1,294 | 1,295 | (0.1)% |
| Operating fleet | 228 | 221 | 7 a/c | 228 | 221 | 7 a/c |
| Regional Operating Statistics:^(c) | | | | | | |
| Revenue passengers (000) | 2,607 | 2,450 | 6.4% | 4,885 | 4,685 | 4.3% |
| RPMs (000,000) "traffic" | 1,263 | 1,030 | 22.6% | 2,306 | 1,910 | 20.7% |
| ASMs (000,000) "capacity" | 1,544 | 1,270 | 21.6% | 2,926 | 2,404 | 21.7% |
| Load factor | 81.8% | 81.1% | 0.7 pts | 78.8% | 79.5% | (0.7) pts |
| Yield ^(d) | 22.64¢ | 26.04¢ | (13.1)% | 22.93¢ | 25.94¢ | (11.6)% |
| RASM ^(d) | 19.14¢ | 21.19¢ | (9.7)% | 18.72¢ | 20.70¢ | (9.6)% |
| Operating fleet | 89 | 78 | 11 a/c | 89 | 78 | 11 a/c |

(a) Except for FTEs, data includes information related to third-party regional capacity purchase flying arrangements.

(b) See a reconciliation of this non-GAAP measure and Note A for a discussion of potential importance of this measure to investors in the accompanying pages.

(c) Data presented includes information related to flights operated by Horizon and third-party carriers.

(d) Certain historical information has been adjusted to reflect the adoption of new accounting standards.

OPERATING SEGMENTS (unaudited)
Alaska Air Group, Inc.

| <i>(in millions)</i> | Three Months Ended June 30, 2018 | | | | | | |
|--|----------------------------------|----------------|--------------|-----------------------|-----------------------------------|------------------------------|---------------|
| | Mainline | Regional | Horizon | Consolidating & Other | Air Group Adjusted ^(a) | Special Items ^(b) | Consolidated |
| Operating revenues | | | | | | | |
| Passenger revenues | \$ 1,711 | \$ 286 | \$ — | \$ — | \$ 1,997 | \$ — | \$ 1,997 |
| CPA revenues | — | — | 137 | (137) | — | — | — |
| Mileage plan other revenue | 99 | 9 | — | — | 108 | — | 108 |
| Cargo and other | 49 | 1 | 1 | — | 51 | — | 51 |
| Total operating revenues | 1,859 | 296 | 138 | (137) | 2,156 | — | 2,156 |
| Operating expenses | | | | | | | |
| Operating expenses, excluding fuel | 1,135 | 249 | 123 | (136) | 1,371 | 39 | 1,410 |
| Economic fuel | 432 | 65 | — | — | 497 | (22) | 475 |
| Total operating expenses | 1,567 | 314 | 123 | (136) | 1,868 | 17 | 1,885 |
| Nonoperating income (expense) | | | | | | | |
| Interest income | 13 | — | — | (3) | 10 | — | 10 |
| Interest expense | (22) | — | (5) | 2 | (25) | — | (25) |
| Interest capitalized | 4 | — | — | — | 4 | — | 4 |
| Other | 1 | (2) | — | — | (1) | — | (1) |
| Total Nonoperating income (expense) | (4) | (2) | (5) | (1) | (12) | — | (12) |
| Income (loss) before income tax | \$ 288 | \$ (20) | \$ 10 | \$ (2) | \$ 276 | \$ (17) | \$ 259 |

| <i>(in millions)</i> | Three Months Ended June 30, 2017 ^(c) | | | | | | |
|--|---|--------------|---------------|-----------------------|-----------------------------------|------------------------------|---------------|
| | Mainline | Regional | Horizon | Consolidating & Other | Air Group Adjusted ^(a) | Special Items ^(b) | Consolidated |
| Operating revenues | | | | | | | |
| Passenger revenues | \$ 1,677 | \$ 268 | \$ — | \$ — | \$ 1,945 | \$ — | \$ 1,945 |
| CPA revenues | — | — | 108 | (108) | — | — | — |
| Mileage plan other revenue | 101 | 8 | — | — | 109 | — | 109 |
| Cargo and other | 45 | 2 | 1 | — | 48 | — | 48 |
| Total operating revenues | 1,823 | 278 | 109 | (108) | 2,102 | — | 2,102 |
| Operating expenses | | | | | | | |
| Operating expenses, excluding fuel | 1,030 | 206 | 116 | (105) | 1,247 | 24 | 1,271 |
| Economic fuel | 304 | 38 | — | — | 342 | 2 | 344 |
| Total operating expenses | 1,334 | 244 | 116 | (105) | 1,589 | 26 | 1,615 |
| Nonoperating income (expense) | | | | | | | |
| Interest income | 10 | — | — | (1) | 9 | — | 9 |
| Interest expense | (24) | — | (3) | 1 | (26) | — | (26) |
| Interest capitalized | 3 | — | 1 | — | 4 | — | 4 |
| Other | — | — | — | — | — | — | — |
| Total Nonoperating income (expense) | (11) | — | (2) | — | (13) | — | (13) |
| Income (loss) before income tax | \$ 478 | \$ 34 | \$ (9) | \$ (3) | \$ 500 | \$ (26) | \$ 474 |

| | Six Months Ended June 30, 2018 | | | | | | |
|--|--------------------------------|----------------|--------------|-----------------------|-----------------------------------|------------------------------|---------------|
| (in millions) | Mainline | Regional | Horizon | Consolidating & Other | Air Group Adjusted ^(a) | Special Items ^(b) | Consolidated |
| Operating revenues | | | | | | | |
| Passenger revenues | \$ 3,153 | \$ 529 | \$ — | \$ — | \$ 3,682 | \$ — | \$ 3,682 |
| CPA revenues | — | — | 247 | (247) | — | — | — |
| Mileage plan other revenue | 197 | 18 | — | — | 215 | — | 215 |
| Cargo and other | 88 | 1 | 2 | — | 91 | — | 91 |
| Total operating revenues | 3,438 | 548 | 249 | (247) | 3,988 | — | 3,988 |
| Operating expenses | | | | | | | |
| Operating expenses, excluding fuel | 2,266 | 488 | 227 | (247) | 2,734 | 70 | 2,804 |
| Economic fuel | 799 | 120 | — | — | 919 | (35) | 884 |
| Total operating expenses | 3,065 | 608 | 227 | (247) | 3,653 | 35 | 3,688 |
| Nonoperating income (expense) | | | | | | | |
| Interest income | 24 | — | — | (6) | 18 | — | 18 |
| Interest expense | (44) | — | (10) | 5 | (49) | — | (49) |
| Interest capitalized | 8 | — | 1 | — | 9 | — | 9 |
| Other | (4) | (9) | — | — | (13) | — | (13) |
| Total Nonoperating income (expense) | (16) | (9) | (9) | (1) | (35) | — | (35) |
| Income (loss) before income tax | \$ 357 | \$ (69) | \$ 13 | \$ (1) | \$ 300 | \$ (35) | \$ 265 |

| | Six Months Ended June 30, 2017 ^(c) | | | | | | |
|--|---|--------------|----------------|-----------------------|-----------------------------------|------------------------------|---------------|
| (in millions) | Mainline | Regional | Horizon | Consolidating & Other | Air Group Adjusted ^(a) | Special Items ^(b) | Consolidated |
| Operating revenues | | | | | | | |
| Passenger revenues | \$ 3,052 | \$ 495 | \$ — | \$ — | \$ 3,547 | \$ — | \$ 3,547 |
| CPA revenues | — | — | 205 | (205) | — | — | — |
| Mileage plan other revenue | 194 | 15 | — | — | 209 | — | 209 |
| Cargo and other | 81 | 3 | 2 | — | 86 | — | 86 |
| Total operating revenues | 3,327 | 513 | 207 | (205) | 3,842 | — | 3,842 |
| Operating expenses | | | | | | | |
| Operating expenses, excluding fuel | 2,030 | 406 | 219 | (203) | 2,452 | 63 | 2,515 |
| Economic fuel | 596 | 75 | — | — | 671 | 12 | 683 |
| Total operating expenses | 2,626 | 481 | 219 | (203) | 3,123 | 75 | 3,198 |
| Nonoperating income (expense) | | | | | | | |
| Interest income | 17 | — | — | (1) | 16 | — | 16 |
| Interest expense | (47) | — | (5) | 1 | (51) | — | (51) |
| Interest capitalized | 7 | — | 1 | — | 8 | — | 8 |
| Other | (1) | — | — | — | (1) | — | (1) |
| Total Nonoperating income (expense) | (24) | — | (4) | — | (28) | — | (28) |
| Income (loss) before income tax | \$ 677 | \$ 32 | \$ (16) | \$ (2) | \$ 691 | \$ (75) | \$ 616 |

(a) The Air Group Adjusted column represents the financial information that is reviewed by management to assess performance of operations and determine capital allocation and does not include certain charges. See Note A in the accompanying pages for further information.

(b) Includes merger-related costs, an employee bonus awarded in January in connection with the Tax Cuts and Jobs Act, and mark-to-market fuel hedge accounting adjustments.

(c) Certain historical information has been adjusted to reflect the adoption of new accounting standards.

GAAP TO NON-GAAP RECONCILIATIONS (unaudited)
Alaska Air Group, Inc.
CASM Excluding Fuel and Special Items Reconciliation

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|-----------------------------|---------------------|---------------------------|---------------------|
| | 2018 | 2017 ^(b) | 2018 | 2017 ^(b) |
| Consolidated: | | | | |
| CASM | 11.20¢ | 10.34¢ | 11.41¢ | 10.66¢ |
| Less the following components: | | | | |
| Aircraft fuel, including hedging gains and losses | 2.82 | 2.21 | 2.74 | 2.28 |
| Special items—merger-related costs and other ^(a) | 0.24 | 0.15 | 0.21 | 0.21 |
| CASM excluding fuel and special items | 8.14¢ | 7.98¢ | 8.46¢ | 8.17¢ |
| Mainline: | | | | |
| CASM | 10.36¢ | 9.48¢ | 10.54¢ | 9.79¢ |
| Less the following components: | | | | |
| Aircraft fuel, including hedging gains and losses | 2.68 | 2.13 | 2.60 | 2.20 |
| Special items—merger-related costs and other ^(a) | 0.25 | 0.17 | 0.23 | 0.24 |
| CASM excluding fuel and special items | 7.43¢ | 7.18¢ | 7.71¢ | 7.35¢ |

(a) Special items includes merger-related costs and an employee bonus awarded in January in connection with the Tax Cuts and Jobs Act.

(b) Certain historical information has been adjusted to reflect the adoption of new accounting standards.

Fuel Reconciliation

| | Three Months Ended June 30, | | | |
|---|-----------------------------|-------------|------------|-------------|
| | 2018 | | 2017 | |
| | Dollars | Cost/Gallon | Dollars | Cost/Gallon |
| <i>(in millions, except for per-gallon amounts)</i> | | | | |
| Raw or "into-plane" fuel cost | \$ 506 | \$ 2.34 | \$ 337 | \$ 1.69 |
| (Gains) losses on settled hedges | (9) | (0.04) | 5 | 0.02 |
| Consolidated economic fuel expense | 497 | 2.30 | 342 | 1.71 |
| Mark-to-market fuel hedge adjustment | (22) | (0.10) | 2 | 0.01 |
| GAAP fuel expense | \$ 475 | \$ 2.20 | \$ 344 | \$ 1.72 |
| Fuel gallons | 216 | | 201 | |

| | Six Months Ended June 30, | | | |
|---|---------------------------|----------------|---------------|----------------|
| | 2018 | | 2017 | |
| | Dollars | Cost/Gallon | Dollars | Cost/Gallon |
| <i>(in millions, except for per gallon amounts)</i> | | | | |
| Raw or "into-plane" fuel cost | \$ 929 | \$ 2.25 | \$ 663 | \$ 1.73 |
| (Gains) losses on settled hedges | (10) | (0.03) | 8 | 0.02 |
| Consolidated economic fuel expense | \$ 919 | \$ 2.22 | \$ 671 | \$ 1.75 |
| Mark-to-market fuel hedge adjustment | (35) | (0.08) | 12 | 0.03 |
| GAAP fuel expense | \$ 884 | \$ 2.14 | \$ 683 | \$ 1.78 |
| Fuel gallons | 413 | | 385 | |

Debt-to-capitalization, adjusted for aircraft operating leases

| (in millions) | June 30, 2018 | December 31, 2017^(a) |
|--|----------------------|--|
| Long-term debt | \$ 1,998 | \$ 2,262 |
| Capitalization of aircraft operating leases ^(b) | 1,883 | 1,671 |
| Adjusted debt | 3,881 | 3,933 |
| Shareholders' equity | 3,593 | 3,460 |
| Total Invested Capital | \$ 7,474 | \$ 7,393 |
| | | |
| Debt-to-capitalization ratio, adjusted for aircraft operating leases | 52% | 53% |

(a) Certain historical information has been adjusted to reflect the adoption of new accounting standards.

(b) Calculated using the present value of remaining aircraft lease payments.

Note A: Pursuant to Regulation G, we are providing reconciliations of reported non-GAAP financial measures to their most directly comparable financial measures reported on a GAAP basis. We believe that consideration of these non-GAAP financial measures may be important to investors for the following reasons:

- By eliminating fuel expense and certain special items (including merger-related costs) from our unit metrics, we believe that we have better visibility into the results of operations and our non-fuel cost-reduction initiatives. Our industry is highly competitive and is characterized by high fixed costs, so even a small reduction in non-fuel operating costs can result in a significant improvement in operating results. In addition, we believe that all domestic carriers are similarly impacted by changes in jet fuel costs over the long run, so it is important for management (and thus investors) to understand the impact of (and trends in) company-specific cost drivers such as labor rates and productivity, airport costs, maintenance costs, etc., which are more controllable by management.
- Cost per ASM (CASM) excluding fuel and certain special items, such as merger-related costs, is one of the most important measures used by management and by the Air Group Board of Directors in assessing quarterly and annual cost performance.
- Adjusted income before income tax and CASM excluding fuel (and other items as specified in our plan documents) are important metrics for the employee incentive plan, which covers the majority of Air Group employees.
- CASM excluding fuel and certain special items is a measure commonly used by industry analysts, and we believe it is the basis by which they compare our airlines to others in the industry. The measure is also the subject of frequent questions from investors.
- Disclosure of the individual impact of certain noted items provides investors the ability to measure and monitor performance both with and without these special items. We believe that disclosing the impact of certain items, such as merger-related costs and mark-to-market hedging adjustments, is important because it provides information on significant items that are not necessarily indicative of future performance. Industry analysts and investors consistently measure our performance without these items for better comparability between periods and among other airlines.
- Although we disclose our passenger unit revenues, we do not (nor are we able to) evaluate unit revenues excluding the impact that changes in fuel costs have had on ticket prices. Fuel expense represents a large percentage of our total operating expenses. Fluctuations in fuel prices often drive changes in unit revenues in the mid-to-long term. Although we believe it is useful to evaluate non-fuel unit costs for the reasons noted above, we would caution readers of these financial statements not to place undue reliance on unit costs excluding fuel as a measure or predictor of future profitability because of the significant impact of fuel costs on our business.

GLOSSARY OF TERMS

Aircraft Utilization - block hours per day; this represents the average number of hours per day our aircraft are in transit

Aircraft Stage Length - represents the average miles flown per aircraft departure

ASMs - available seat miles, or “capacity”; represents total seats available across the fleet multiplied by the number of miles flown

CASM - operating costs per ASM, or "unit cost"; represents all operating expenses including fuel and special items

CASMex - operating costs excluding fuel and special items per ASM; this metric is used to help track progress toward reduction of non-fuel operating costs since fuel is largely out of our control

Debt-to-capitalization ratio - represents adjusted debt (long-term debt plus the present value of future operating lease payments) divided by total equity plus adjusted debt

Diluted Earnings per Share - represents earnings per share (EPS) using fully diluted shares outstanding

Diluted Shares - represents the total number of shares that would be outstanding if all possible sources of conversion, such as stock options, were exercised

Economic Fuel - best estimate of the cash cost of fuel, net of the impact of our fuel-hedging program

Free Cash Flow - total operating cash flow generated less cash paid for capital expenditures

Load Factor - RPMs as a percentage of ASMs; represents the number of available seats that were filled with paying passengers

Mainline - represents flying Boeing 737 and Airbus 320 family jets and all associated revenues and costs

Productivity - number of revenue passengers per full-time equivalent employee

RASM - operating revenue per ASMs, or "unit revenue"; operating revenue includes all passenger revenue, freight & mail, Mileage Plan and other ancillary revenue; represents the average total revenue for flying one seat one mile

Regional - represents capacity purchased by Alaska from Horizon, SkyWest and PenAir. In this segment, Regional records actual on-board passenger revenue, less costs such as fuel, distribution costs, and payments made to Horizon, SkyWest and PenAir under the respective capacity purchased arrangement (CPAs). Additionally, Regional includes an allocation of corporate overhead such as IT, finance, other administrative costs incurred by Alaska and on behalf of Horizon.

RPMs - revenue passenger miles, or "traffic"; represents the number of seats that were filled with paying passengers; one passenger traveling one mile is one RPM

Yield - passenger revenue per RPM; represents the average revenue for flying one passenger one mile

Alaska Air Group

Investor Update - July 26, 2018

References in this update to “Air Group,” “Company,” “we,” “us,” and “our” refer to Alaska Air Group, Inc. and its subsidiaries, unless otherwise specified.

This update includes forecasted operational and financial information for our consolidated operations. Our disclosure of operating cost per available seat mile, excluding fuel and other items, provides us (and may provide investors) with the ability to measure and monitor our performance without these items. The most directly comparable GAAP measure is total operating expenses per available seat mile. However, due to the large fluctuations in fuel prices, we are unable to predict total operating expenses for any future period with any degree of certainty. In addition, we believe the disclosure of fuel expense on an economic basis is useful to investors in evaluating our ongoing operational performance. Please see the cautionary statement under “Forward-Looking Information.”

We are providing information about estimated fuel prices and our hedging program. Management believes it is useful to compare results between periods on an “economic basis.” *Economic fuel expense* is defined as the raw or “into-plane” fuel cost less any cash we receive from hedge counterparties for hedges that settle during the period, offset by the recognition of premiums originally paid for those hedges that settle during the period. Economic fuel expense more closely approximates the net cash outflow associated with purchasing fuel for our operation.

Forward-Looking Information

This update contains forward-looking statements subject to the safe harbor protection provided by Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995. These statements relate to future events and involve known and unknown risks and uncertainties that may cause actual outcomes to be materially different from those indicated by any forward-looking statements. For a comprehensive discussion of potential risk factors, see Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2017, as well as in other documents filed by the Company with the SEC after the date thereof. Some of these risks include general economic conditions, increases in operating costs including fuel, competition, labor costs and relations, our indebtedness, inability to meet cost reduction goals, seasonal fluctuations in our financial results, an aircraft accident, changes in laws and regulations, and risks inherent in the achievement of anticipated synergies and the timing thereof in connection with the acquisition of Virgin America. All of the forward-looking statements are qualified in their entirety by reference to the risk factors discussed therein. We operate in a continually changing business environment, and new risk factors emerge from time to time. Management cannot predict such new risk factors, nor can it assess the impact, if any, of such new risk factors on our business or events described in any forward-looking statements. We expressly disclaim any obligation to publicly update or revise any forward-looking statements after the date of this report to conform them to actual results. Over time, our actual results, performance or achievements will likely differ from the anticipated results, performance or achievements that are expressed or implied by our forward-looking statements, and such differences might be significant and materially adverse.

AIR GROUP - CONSOLIDATED

Forecast Information

| | Forecast Full Year 2018 | Full Year 2017 As Adjusted ^(a) | % Change | Prior Guidance June 15, 2018 |
|---|----------------------------|--|----------|---------------------------------|
| Capacity (ASMs in millions) | 65,780 - 65,930 | 62,072 | ~ 6.1% | 65,950 - 66,100 |
| Cost per ASM excluding fuel and special items (cents) | 8.50¢ - 8.53¢ | 8.25¢ | ~ 3.2% | 8.51¢ - 8.56¢ |
| Fuel gallons (millions) | 843 | 797 | ~ 5.8% | 845 |

| | Forecast Q3 2018 | Q3 2017 As Adjusted ^(a) | % Change | Prior Guidance April 23, 2018 |
|---|---------------------|---------------------------------------|-----------------|----------------------------------|
| Capacity (ASMs in millions) | 17,095 - 17,145 | 16,164 | ~ 5.9% | ~ 6.0% |
| Revenue per ASM (cents) ^(a) | 12.66¢ - 13.06¢ | 13.06¢ | ~ (3.0)% - 0.0% | n/a |
| Cost per ASM excluding fuel and special items (cents) | 8.36¢ - 8.41¢ | 8.00¢ | ~ 4.9% | 8.31¢ - 8.36¢ |
| Fuel gallons (millions) | 218 | 207 | ~ 5.3% | n/a |
| Economic fuel cost per gallon ^(b) | \$2.30 | \$1.80 | ~ 27.8% | n/a |

(a) RASM and CASMex in the preceding forecast information reflect the impacts of the updated accounting standards, effective for the Company January 1, 2018. Information not impacted by the updated accounting standards (Fuel Gallons and Economic fuel cost per gallon) has not been restated. Additionally, certain reclassifications have been made to prior year financial statements to conform to classifications used in the current year.

(b) Our economic fuel cost per gallon estimate for the third quarter includes the following per-gallon assumptions: crude oil cost—\$1.65 (approximately \$69 per barrel), refining margin—50 cents, benefit of settled hedges—5 cents, with the remaining difference due to taxes and other into-plane costs.

2018 Forecasted Capacity and CASMex by Quarter

The following table shows 2018 quarterly forecasted capacity by segment and forecasted consolidated CASMex with percent change on an adjusted basis from the same period in the prior year. Certain reclassifications have been made to prior year financial information to conform to classifications used in the current year.

| | Actual | | Forecast | | |
|---------------------------------|--------|---------|---------------|---------------|---------------|
| | Q1 | Q2 | Q3 | Q4 | Full Year |
| Mainline ASMs | 6.3% | ~ 6.6% | ~ 5.0% | ~ 1.5% | ~ 5.0% |
| Regional ASMs | 21.8% | ~ 21.6% | ~ 18.5% | ~ 20.0% | ~ 20.0% |
| Total Air Group ASMs | 7.5% | ~ 7.8% | ~ 5.9% | ~ 3.0% | ~ 6.1% |
| Prior Guidance April 23, 2018 | | | ~ 6.0% | ~ 4.0% | ~ 6.5% |
| CASMex (cents) | 8.81¢ | 8.14¢ | 8.36¢ - 8.41¢ | 8.72¢ - 8.77¢ | 8.50¢ - 8.53¢ |
| 2017 CASMex (cents) as adjusted | 8.38¢ | 7.98¢ | 8.00¢ | 8.68¢ | 8.25¢ |

Capacity and Capital Expenditures Forecast

The guidance below is based on our current expectation of capacity growth and capital expenditures.

| <i>(in millions, except %)</i> | 2018 | 2019 | 2020 |
|---------------------------------------|-------------|-------------|-------------|
| Capacity (ASMs) growth | 6.1% | ~ 2% | ~ 4% |
| Targeted capital expenditures | ~\$1,000 | ~\$750 | ~\$750 |

Nonoperating Expense

We expect that our consolidated nonoperating expense will be approximately \$15 million in the third quarter of 2018.

Effective Tax Rate

We expect the 2018 full year effective tax rate to be approximately 25%.

Future Fuel Hedge Positions

All of our future oil positions are call options, which are designed to effectively cap the cost of the crude oil component of our jet fuel purchases. Our crude oil positions are as follows:

| | Approximate % of Expected Fuel Requirements | Weighted-Average Crude Oil Price per Barrel | Average Premium Cost per Barrel |
|-----------------------|--|--|--|
| Third Quarter 2018 | 50% | 65 | 1 |
| Fourth Quarter 2018 | 50% | 68 | 1 |
| Remainder 2018 | 50% | \$ 67 | \$ 1 |
| First Quarter 2019 | 40% | 70 | 1 |
| Second Quarter 2019 | 30% | 72 | 2 |
| Third Quarter 2019 | 20% | 74 | 2 |
| Fourth Quarter 2019 | 10% | 77 | 3 |
| Full Year 2019 | 25% | \$ 72 | \$ 2 |