Annual Report

AMERICAN AIRLINES, Inc.

YEAR ENDED DECEMBER 31, 1945

1945 Annual Report to the Stockholders of American Airlines, Inc.

AMERICAN AIRLINES, *Inc.*

OFFICES:

General Offices: 100 East 42nd Street, New York 17, New York

Corporate Office, 927 Market Street, Wilmington, Delaware

Transfer Agent....Schroder Trust Company, New York 5, N. Y.

Registrar.....Guaranty Trust Company of New York

General Counsel.....Douglas and Proctor, Washington, D. C.

AMERICAN AIRLINES, Inc.

DIRECTORS

Harold T. Ames
Harry E. Benedict
James Bruce
Edward H. Butler
Amon G. Carter
Ralph S. Damon
Silliman Evans
John W. Farley
Thomas Stevens Hammond
Chandler Hovey
A. N. Kemp
Walter Scott McLucas
O. M. Mosier
Edgar Monsanto Queeny
C. R. Smith

OFFICERS

C. R. Smith,
Chairman of the Board

Ralph S. Damon,
President

VICE-PRESIDENTS

Amos Culbert
R. E. S. Deichler
Terrell C. Drinkwater
L. G. Fritz
William Littlewood
O. M. Mosier
Charles A. Rheinstrom
Rex W. D. Smith, Jr.
P. P. Willis

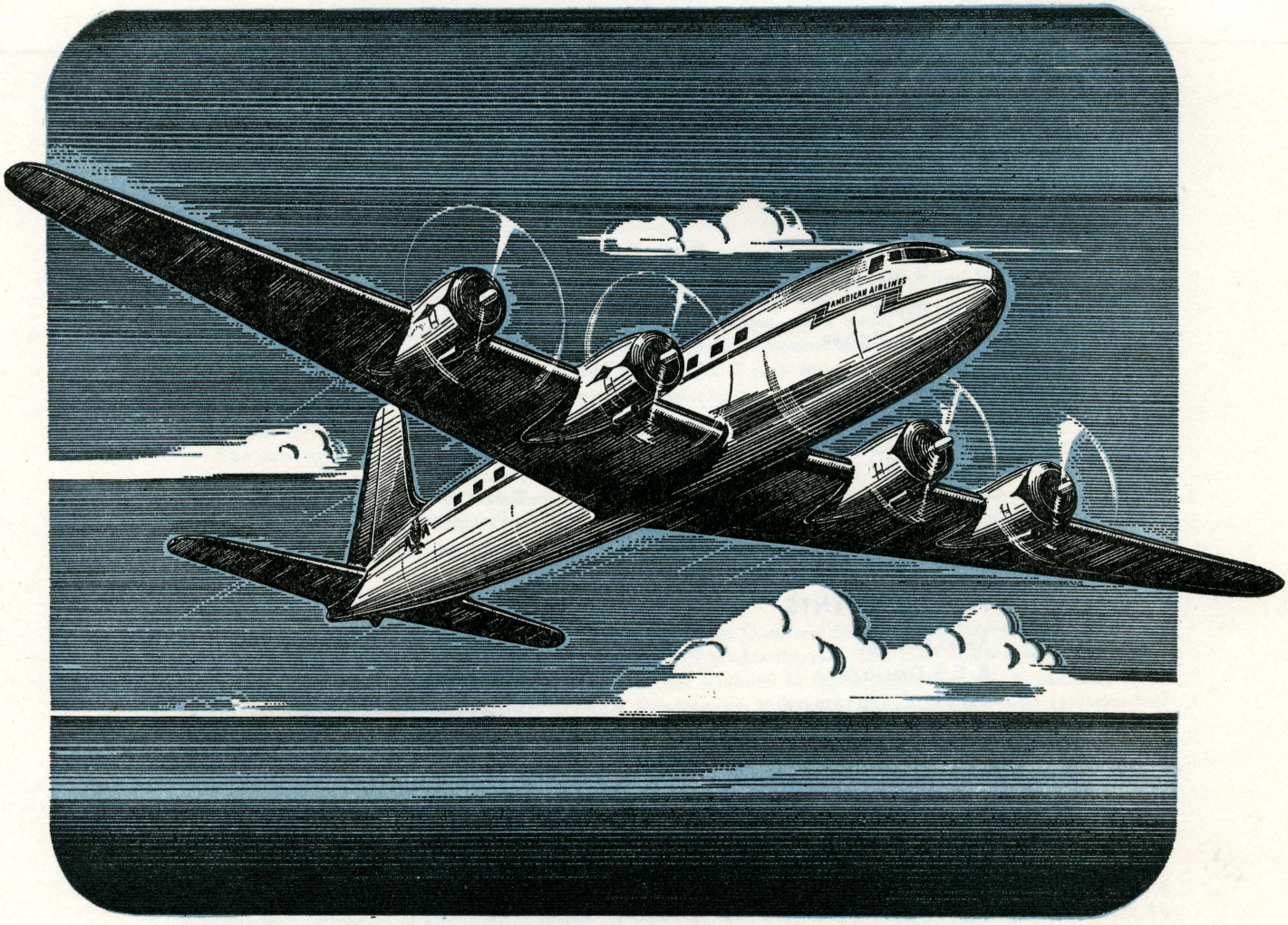
TREASURER

H. K. Rulison

SECRETARY

C. W. Jacob

Willis G. Lipscomb, Assistant Vice President
W. H. Miller, Assistant Vice President
Carlene Roberts, Assistant Vice President
P. G. Larie, Comptroller and Assistant Treasurer
C. H. Kibbee, Assistant Treasurer
V. J. Long, Assistant Secretary and Assistant Treasurer
A. R. Bone, Regional Vice President
W. Nelson Bump, Regional Vice President
L. W. King, Regional Vice President
M. D. Miller, Regional Vice President
C. R. Speers, Jr., Regional Vice President



Douglas DC-6 Flagships will be joining the American Airlines Fleet this Fall

To The Stockholders

New York, N. Y., March 20, 1946

World War II ended during the year. The record of the participation of American, and of men and women from American, is known, and will constitute a memorable page in the history of the organization. We continue to operate contract services for the War Department but it is expected that these will be terminated during the first half of 1946. The job now ahead is reconversion and expansion to meet the requirements of peacetime operation.

The war tremendously accelerated technical advance. Developments such as radar, thermal wing de-icing, jet propulsion, high-octane fuels, advances in aerodynamics and increased efficiency of power plants will increase the safety and efficiency of air transportation. The Company will not lag behind in orderly adaptation and adoption of these more effective devices.

During the year, acquisition of control of American Export Airlines was approved by the Civil Aeronautics Board and 51.4 percent of the stock in that company was acquired. A certificate to serve Denmark, Eire, Finland, Germany, Greenland, Holland, Iceland, Labrador, Newfoundland, Norway, Poland, Russia, Sweden and the United Kingdom was awarded to American Export. The name American Export Airlines has been changed to American Overseas Airlines. Operations to Denmark, Eire, Holland, Iceland, Newfoundland, Sweden, and the United Kingdom have been inaugurated. It is anticipated that operations to Germany, Norway and Scotland will be instituted soon. The rate of compensation for the transportation of mail by American Overseas Airlines has not yet been established by the Civil Aeronautics Board. Assuming that the Board, at the time of fixing a definitive mail rate for that company, adheres to the principles which it has generally applied in rate proceedings, the income statement of the company would show a profit for the 1945 operations of $211,551.

EARNINGS

Net profit carried to surplus in 1945 was $4,339,458 compared with $4,396,163 for 1944. The 1944 figure is after provision of $1,000,000 as reserve for transition to peacetime operations. The reserve heretofore established is deemed sufficient and was not increased in 1945.

Net earnings for 1945 before provision for Federal income taxes, were $8,139,458 as compared with $8,446,163 after provision of the $1,000,000 reserve in 1944. Provision for 1945 Federal Income Taxes was $3,800,000, compared with $4,050,000 for 1944.

DIVIDENDS AND SURPLUS

Common stock dividend No. 6, $1.00 per share, was paid December 22, 1945, on 1,290,495 shares of record on December 7, 1945.

Surplus, after payment of dividends, was $19,689,737 at December 31, 1945, compared with $16,232,736 at the close of 1944. Excess of earnings over dividends in 1945 added $3,045,445 to Earned Surplus; Paid-In Surplus was increased $411,556 by conversion of 4,692 shares of Prior Preferred stock.

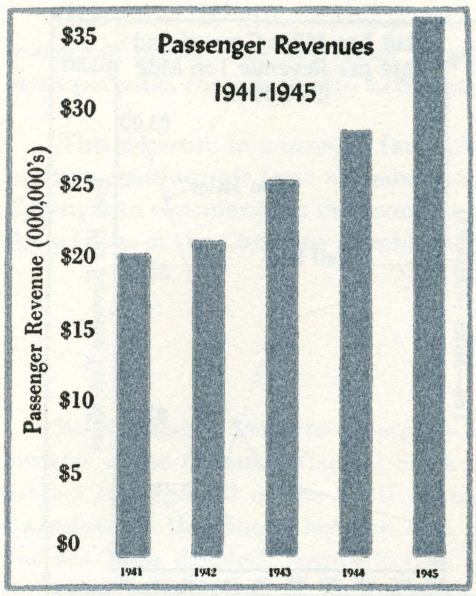
CAPITAL EXPENDITURES

During the war only aircraft of pre-war design were available for civil operation. Now, more effective aircraft, utilized by the military services during the war, have been acquired. Progress of the industry, and of American, is dependent upon the adoption and use of aircraft of most effective type and the Company has entered firm orders for future delivery of aircraft of advanced design and performance.

The Douglas C54 was the outstanding military transport. Fifty are being acquired to be modified and serve as effective transition airplanes. The Company has also ordered 50 Douglas DC6 aircraft a number of which will be delivered during the latter part of 1946. These will be high performance, four-engined aircraft of advanced design. In addition, American has participated in the development of a high performance, twin-engined aircraft and plans to acquire one hundred aircraft of that type, delivery commencing in 1947.

Total cost of the equipment above referred to, including parts, will be approximately $75,000,000, and additional equipment will be required. Also substantial expenditures will arise in providing hangars, offices and ground equipment. Toward meeting these requirements it is proposed to secure during 1946 approximately $80,000,000 of additional funds through the sale of debentures and convertible Preferred Stock. Out of the proceeds of such financing it is intended to repay present bank loans aggregating $25,000,000 which were negotiated in February 1946.

To provide for present requirements of American Overseas Airlines, that company has recently borrowed $10,000,000, substantially on the same terms as the loan of American Airlines. Repayment of the American Overseas Airlines' loan is guaranteed by American Airlines.



In 1945 the Company operated 47,988,164 revenue airplane miles, with operating revenue of $47,416,000, compared with 34,581,949 miles flown in 1944 and operating revenue of $39,244,012. Passenger revenue increased from $29,338,231 in 1944 to $37,317,430 in 1945; mail revenue decreased from $6,685,282 in 1944 to $5,981,051 in 1945 and express and freight revenue increased from $2,529,922 in 1944 to $3,384,573 in 1945.

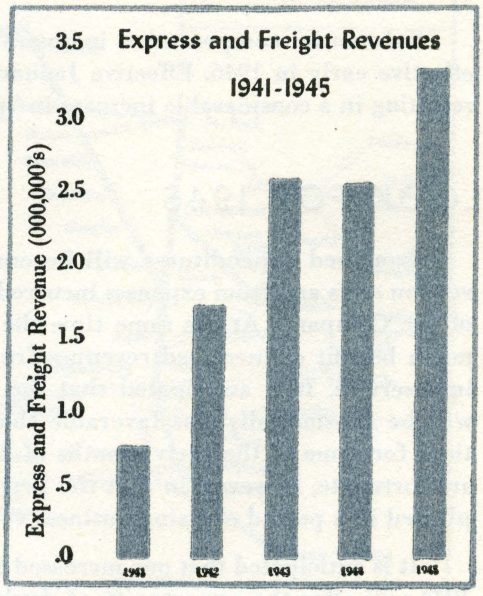
Rate reductions during the year reduced the average revenue yield from 54 cents per ton-mile in 1944 to 47 cents in 1945.

Passenger fares were reduced on August 20, 1945 to 4.5 cents per mile. Average fare for 1944 was 5.05 cents per mile.

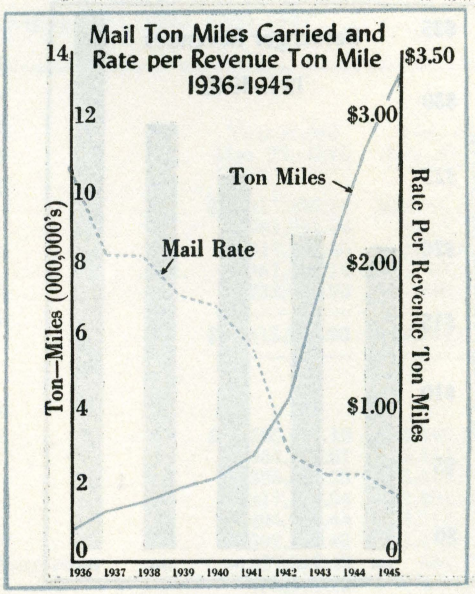
On January 1, 1945, the Civil Aeronautics Board entered a "show cause order", affecting American and three other domestic air carriers, requiring submission of proof that the rate for transporting air mail should not be reduced from 60 cents per ton mile to 32 cents per ton mile, effective January 1, 1945. Such reduction, in the opinion of the Company, was not and is not justified and proof was submitted on that basis. The show cause order was amended to 45 cents per ton mile and that rate became effective as of January 1, 1945.

Air express showed average revenue of 49 cents per ton mile in 1945. Rates were reduced on January 1, 1946 to provide estimated revenues of 45 cents per ton mile.

Continued progress was made in the development of Airfreight, inaugurated by the Com-



pany in 1944 as the industry's first air freight service. Experiments were conducted in the carriage of perishable produce and fruit by air. The carriage of air freight under contract was tested. On the basis of this experience, American plans to introduce the operation of improved types of aircraft equipped specifically for cargo transportation.



OPERATING EXPENSES

The 1945 operating costs were 81.9 cents per airplane mile, compared with 86.2 cents in 1944. Specific elements of cost increased substantially during the year, but overall mileage costs showed reduction, largely through the economic benefits of increased operation.

Substantial compensation increases were made during 1945; further increases became effective early in 1946. Effective January 1, 1946, the work week was reduced to 40 hours, resulting in a considerable increase in "per hour" compensation and cost.

OUTLOOK FOR 1946

Increased expenditures will be encountered in the first quarter, arising from reconversion costs and from expenses incurred in preparation for the domestic expansion program of the Company. At the same time the Company will not during the first quarter receive much benefit of increased revenues from the fleet of four-engined aircraft now being put into service. It is anticipated that the results of operations for the first quarter of 1946 will be substantially less favorable than the comparable period of 1945 and that operations for some of the early months of 1946 may result in loss. The industry and American are fortunate, however, in that the period of reconversion will be short and will be accomplished in a period of rising business volume.

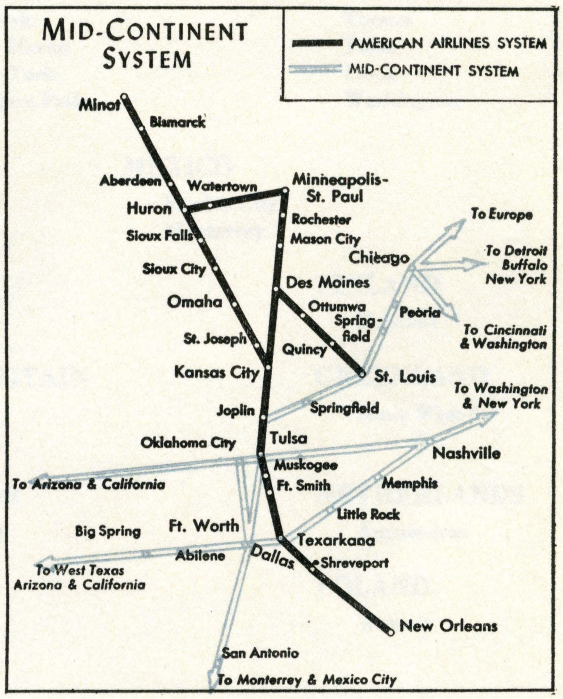
It is anticipated that our increased transportation capacity for the full twelve months of 1946 will offer the opportunity of doubling the number of passengers transported in 1945. The lower passenger fares of 1946 will, however, serve to reduce the average gross revenue per passenger.

The trend for 1946, indicates a materially increased volume of business but at a lower margin of profit. This will result largely from the fact that air passenger fares are now 4.5 cents per mile, compared with 5.05 cents per mile in the early part of 1945.

This decrease in passenger fares places the air transportation industry in superior competitive position; air fares are now generally at the same level as rail plus pullman charges. Taking into consideration the economy of its fare and the backlog of transportation demand, the services of the Company should operate with reasonable load factors throughout the year.

EXPANSION AND DEVELOPMENT

In September 1945 the Company entered into a contract for the acquisition of 50.75 percent of the Common Capital Stock of Mid-Continent Airlines. Acquisition of control is subject to approval of the Civil Aeronautics Board. A hearing has been held before an Examiner of the Board but the case has not been decided. Acquisition is proposed on the basis of exchanging one share of present American Common Stock for four shares of Mid-Continent stock and that rate of exchange will be offered to all stockholders of Mid-Continent. If this acquisition is approved by the Board and all stockholders of Mid-Continent accept the exchange, 97,350 shares of American's present Common Stock will be issued in exchange for 389,398.6 shares of Mid-Continent.



Mid-Continent routes extend into ten states and serve twenty-five communities with a population of 4,778,813 persons of which twenty-one cities and 3,156,290 persons are not now served by American including such important cities as New Orleans, Shreveport, Omaha, Des Moines, Kansas City, Minneapolis and Saint Paul.

ORGANIZATION

In June 1945, Mr. A. N. Kemp, who served as President during the war, resigned as an officer of the Company but continues to serve as director. Mr. Ralph S. Damon, formerly Vice President and General Manager, was elected President.

C. R. Smith, President of the Company from 1934 to 1942, returned from service with the Army Air Forces and was elected Chairman of the Board and Chief Executive Officer.

Following their discharge from the Armed Services, Lawrence G. Fritz was elected Vice President—Operations, R. E. S. Deichler, Vice President—Administration, Rex W. D. Smith, Jr., Vice President—Public Relations, Charles R. Speers, Jr., Regional Vice President —New York, and Chandler H. Kibbee, Assistant Treasurer. Mr. P. P. Willis, who has handled the Company's advertising for years, was elected Vice President—Advertising. Miss Carlene Roberts was elected Assistant Vice President—Washington Office.

The Board of Directors wishes to express its appreciation of the continued support and cooperation of the stockholders and of the effort, initiative and spirit of the entire personnel of the Company.

Respectfully submitted,

R S Damon

President

C R Smith

Chairman of the Board

AMERICAN AIRLINES SYSTEM
CITIES AUTHORIZED FOR SERVICE

UNITED STATES

Abilene
Akron
Albany
Ann Arbor
Baltimore
Battle Creek
Big Spring
Binghamton
Boston
Bridgeport
Bristol
Buffalo
Charleston-Dunbar
Chicago
Cincinnati
Clarksburg
Cleveland
Columbus
Corning
Dallas
Dayton
Detroit
Douglas
El Paso
Elkins
Elmira
Erie
Fort Worth
Hartford
Huntington
Indianapolis
Jackson
Joplin
Kalamazoo
Knoxville
Little Rock
Los Angeles
Louisville
Lynchburg
Memphis
Nashville
Newark
New Haven
New York
Niagara Falls
Oklahoma City
Parkersburg
Peoria
Philadelphia
Phoenix
Providence
Roanoke
Rochester
St. Louis
San Antonio
San Diego
Scranton-Wilkes Barre
South Bend
Springfield, Ill.
Springfield, Mass.
Springfield, Mo.
Syracuse
Texarkana
Tucson
Tulsa
Utica
Washington

CANADA

Toronto
Windsor

MEXICO

Mexico City
Monterrey

DENMARK

Copenhagen

EIRE

Shannon

FINLAND

Helsinki

GERMANY

Berlin
Frankfurt

GREAT BRITAIN

Glasgow
London

GREENLAND

Bluie West 1

ICELAND

Reykjavik

LABRADOR

Goose Bay

NETHERLANDS

Amsterdam

NEWFOUNDLAND

Gander

NORWAY

Oslo

POLAND

Warsaw

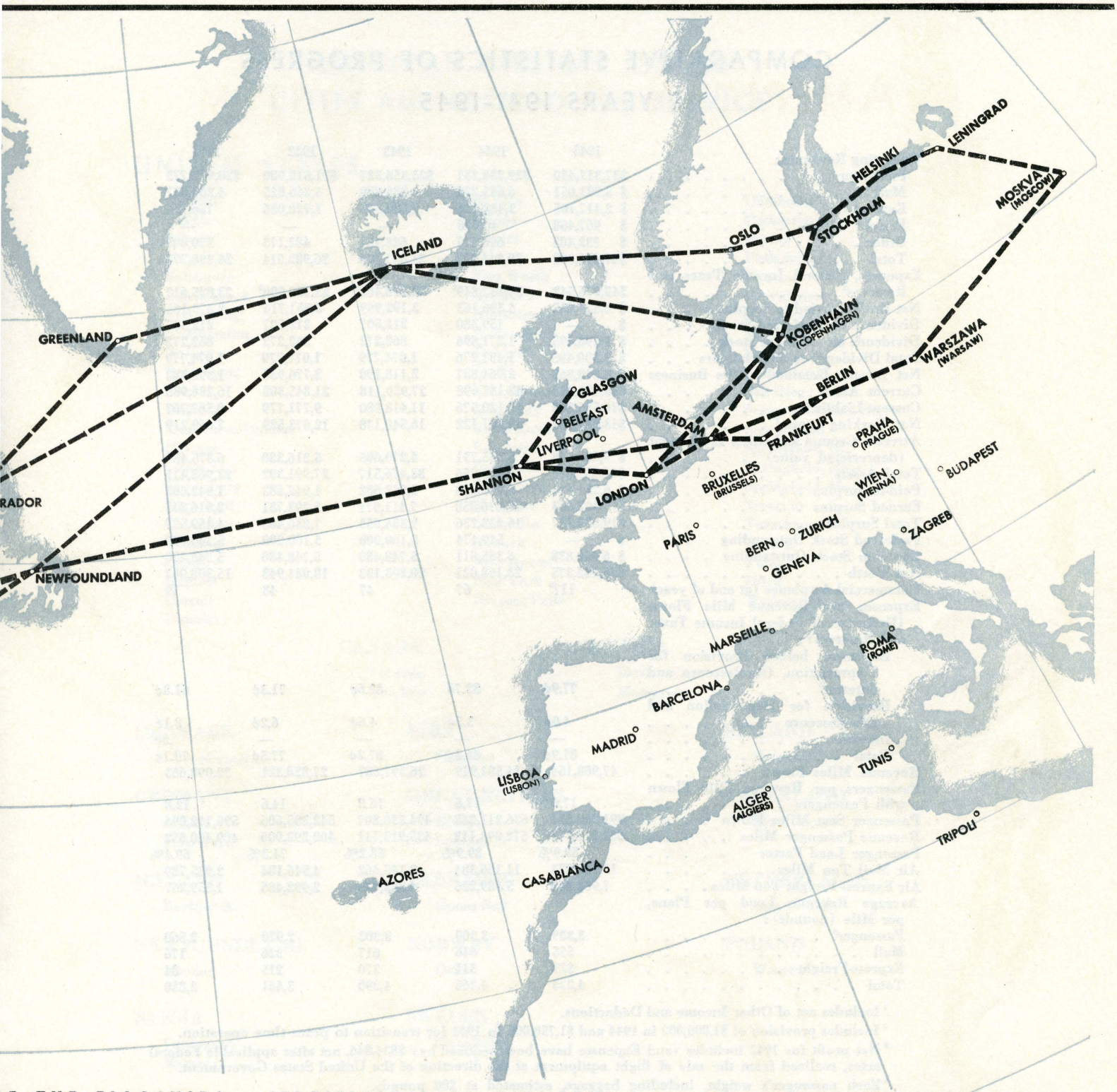
RUSSIA

Leningrad
Moscow

SWEDEN

Stockholm

AMERICAN AIRLINES SYSTEM



OF THE FLAGSHIPS • CERTIFICATED TO SERVE

MARK • EIRE • ENGLAND • FINLAND • GERMANY • GREENLAND • ICELAND • MEXICO

NEWFOUNDLAND • NORWAY • POLAND • RUSSIA • SCOTLAND • SWEDEN • UNITED STATES

AMERICAN AIRLINES

AMERICAN OVERSEAS AIRLINES

COMPARATIVE STATISTICS OF PROGRESS

YEARS 1941-1945

	1945	1944	1943	1942	1941
Operating Revenues:					
Passenger	$37,317,430	$29,338,231	$23,356,327	$21,512,980	$20,922,773
Mail	$ 5,981,051	6,685,282	4,886,389	3,266,825	4,269,881
Express	$ 2,417,105	2,483,246	2,580,562	1,720,036	756,116
Freight	$ 967,468	46,676	—	—	—
Other	$ 732,408	690,577	628,152	482,173	350,008
Total	$47,416,000	39,244,012	31,451,430	26,982,014	26,298,778
Expenses, Federal Income Taxes and Reserves[1]	$43,076,542	34,847,849[2]	28,258,461[2]	23,130,300[3]	23,825,617
Net Profit Carried to Surplus	$ 4,339,458	4,396,163	3,192,969	3,851,714[3]	2,473,161
Dividends on Preferred Stock	$ —	159,380	212,507	212,507	212,507
Dividends on Common Stock	$ 1,290,495	1,271,896	862,272	862,272	862,272
Total Dividends to Stockholders	$ 1,290,495	1,431,276	1,074,779	1,074,779	1,074,779
Net Income Retained in the Business	$ 3,048,963	2,964,887	2,118,190	2,776,935	1,398,382
Current Assets	$30,420,420	32,187,698	27,959,118	21,845,308	16,236,986
Current Liabilities	$16,536,268	13,120,576	11,418,980	9,771,779	8,567,767
Net Working Capital	$13,884,152	19,067,122	16,540,138	12,073,529	7,669,219
Aircraft, Ground and Other Equipment (depreciated value)	$ 9,689,548	5,385,731	4,270,605	5,216,380	6,875,487
Total Assets	$45,857,823	39,259,256	33,476,517	27,991,392	23,968,411
Paid-in Surplus	$ 6,267,434	5,855,878	1,942,682	1,942,682	1,942,682
Earned Surplus	$13,422,303	10,376,858	7,411,971	5,293,781	2,516,845
Total Surplus	$19,689,737	16,232,736	9,354,653	7,236,463	4,459,527
Preferred Stock Outstanding	$ —	549,474	5,100,000	5,100,000	5,100,000
Common Stock Outstanding	$ 6,452,838	6,385,811	5,748,480	5,748,480	5,748,480
Net Worth	$26,142,575	23,168,021	20,203,133	18,084,943	15,308,007
Commercial Airplanes (at end of year)	117[5]	67	47	43	79
Expenses per Revenue Mile Flown (Exclusive of Federal Income Taxes and Reserves):					
Expenses, before Provision for Depreciation, Obsolescence and Interest[1]	77.9¢	82.7¢	82.6¢	71.3¢	61.8¢
Provision for Depreciation and Obsolescence	4.0¢	3.5¢	4.6¢	6.2¢	8.1¢
Interest	—	—	—	—	.2¢
Total	81.9¢	86.2¢	87.2¢	77.5¢	70.1¢
Revenue Miles Flown	47,988,164	34,581,949	26,397,687	27,828,321	32,098,663
Passengers per Revenue Mile Flown with Passengers	17.6	17.6	16.8	14.6	12.8
Passenger Seat Miles Flown	891,243,514	636,211,268	494,320,807	542,385,606	590,172,096
Revenue Passenger Miles	801,219,311	572,094,112	435,913,741	402,298,900	409,400,652
Passenger Load Factor	89.9%	89.9%	88.2%	74.2%	69.4%
Air Mail Ton Miles	13,326,023	11,166,384	8,145,462	4,546,184	2,935,789
Air Express-Freight Ton Miles	7,903,845	5,389,226	4,882,115	2,992,486	1,359,267
Average Revenue Load per Plane, per Mile (pounds):					
Passenger[4]	3,339	3,309	3,303	2,920	2,560
Mail	555	646	617	326	176
Express-Freight	329	311	370	215	84
Total	4,223	4,266	4,290	3,461	2,820

[1] Includes net of Other Income and Deductions.

[2] Includes provision of $1,000,000 in 1944 and $1,750,000 in 1943 for transition to peace time operation.

[3] Net profit for 1942 includes (and Expenses have been reduced by) $834,846, net after applicable Federal taxes, realized from the sale of flight equipment at the direction of the United States Government.

[4] Each passenger's weight, including baggage, estimated at 200 pounds.

[5] On hand 65 DC3's owned, 24 DC3's leased, and 28 C54's which the company intends to purchase and were being modified at that date. Does not include aircraft for training or experimental purposes.

ARTHUR YOUNG & COMPANY
ACCOUNTANTS AND AUDITORS
1 CEDAR STREET
NEW YORK 5, N. Y.

NEW YORK
CHICAGO
DALLAS
KANSAS CITY
LOS ANGELES
MILWAUKEE
PITTSBURGH
TULSA

TORONTO
MONTREAL
—
LONDON
PARIS

To the Board of Directors and Stockholders
American Airlines, Inc.:

We have examined the consolidated balance sheet of AMERICAN AIRLINES, INC. AND CONSOLIDATED SUBSIDIARY at December 31, 1945 and the consolidated statements of profit and loss and surplus for the year then ended, have reviewed the system of internal control and the accounting procedures of the Companies and, without making a detailed audit of the transactions, have examined or tested accounting records of the Companies and other supporting evidence, by methods and to the extent we deemed appropriate. It was not practicable to confirm receivables from the U. S. Government for services performed under war contracts and for air travel, etc., but we have satisfied ourselves by other means as to the substantial accuracy thereof. Our examination was made in accordance with generally accepted auditing standards applicable in the circumstances and included all procedures which we considered necessary.

In our opinion, the accompanying consolidated balance sheet and consolidated statements of profit and loss and surplus present fairly the position of American Airlines, Inc. and Consolidated Subsidiary at December 31, 1945, and the results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

ARTHUR YOUNG & COMPANY

New York, N. Y.
March 12, 1946.

AMERICAN AIRLINES, INC.

CONSOLIDATED

AT DECEMBER 31, 1945

ASSETS

	Dec. 31, 1945	Dec. 31, 1944
CURRENT ASSETS:		
Cash on hand and demand deposits	$11,993,858.48	$ 8,948,418.66
Marketable securities, at cost (approximately market):		
U. S. Government	$ 7,191,127.50	$12,939,225.00
Canadian Government	226,250.00	136,350.00
	$ 7,417,377.50	$13,075,575.00
Accounts receivable		
U. S. Government:		
For services performed at cost under war contracts	$ 2,858,955.08	$ 5,138,083.66
Less: Advance payments received	—	1,286,769.00
	$ 2,858,955.08	$ 3,851,314.66
For the transportation of air mail	1,448,849.73	1,366,999.33
For air travel, etc.	1,128,572.24	1,139,045.33
Air travel plan subscribers	1,390,629.11	792,061.88
Other airline companies and agents—traffic and express balances	1,532,714.80	1,809,734.35
Other trade accounts	770,332.78	446,345.76
Indebtedness of employees	114,436.60	78,673.35
	$ 9,244,490.34	$ 9,484,174.66
Less: Reserve for doubtful accounts receivable	133,227.64	154,183.63
	$ 9,111,262.70	$ 9,329,991.03
Advance to American Overseas Airlines, Inc. (repaid March 8, 1946)	$ 1,000,000.00	$ —
Inventories—parts and supplies, at the lower of cost or market	$ 897,921.79	$ 833,713.71
TOTAL CURRENT ASSETS	$30,420,420.47	$32,187,698.40
INVESTMENTS AND SPECIAL FUNDS:		
Investments in subsidiaries not consolidated, at cost (Note 1):		
American Overseas Airlines, Inc.	$ 3,000,000.00	$ —
Other	651,000.00	500,000.00
Miscellaneous investments in connection with operations, at cost	118,720.81	43,552.72
Cash deposits in connection with acquisition of airplanes	894,000.00	275,000.00
Other special deposits	110,837.11	53,540.00
	$ 4,774,557.92	$ 872,092.72
FLIGHT EQUIPMENT, AT COST	$13,645,586.23	$ 9,363,870.61
Less: Reserve for obsolescence and depreciation	7,753,720.23	6,738,337.40
	$ 5,891,866.00	$ 2,625,533.21
LAND, BUILDINGS AND OTHER EQUIPMENT, AT COST (Note 2)	$ 6,842,979.42	$ 5,294,375.89
Less: Reserve for depreciation	3,045,297.82	2,534,178.10
	$ 3,797,681.60	$ 2,760,197.79
NON-OPERATING PROPERTY AND EQUIPMENT, AT ESTIMATED REALIZABLE VALUE	$ 21,320.00	$ 21,320.00
LONG TERM OPERATING PROPERTY PREPAYMENTS, LESS AMORTIZATION	$ 613,938.15	$ 513,429.05
DEFERRED CHARGES:		
Prepaid rents and insurance	$ 212,935.69	$ 154,895.79
Other deferred charges	125,103.56	124,089.29
	$ 338,039.25	$ 278,985.08
	$45,857,823.39	$39,259,256.25

Explanatory notes are attached hereto.

AND CONSOLIDATED SUBSIDIARY

BALANCE SHEETS

AND DECEMBER 31, 1944

LIABILITIES, CAPITAL STOCK AND SURPLUS

	Dec. 31, 1945	Dec. 31, 1944
CURRENT LIABILITIES:		
Accounts payable	$ 4,291,957.30	$ 2,435,161.34
Other airline companies—traffic balances payable	2,416,541.94	2,028,803.10
Air travel plan subscribers' deposits	4,277,197.87	3,110,453.88
Accrued salaries and wages	618,694.71	607,915.82
Accrued Federal income taxes (Note 3)	4,064,889.55	4,139,748.41
Other accrued taxes	252,870.20	365,378.78
Other accrued liabilities	614,116.73	433,114.21
TOTAL CURRENT LIABILITIES	$16,536,268.30	$13,120,575.54
UNEARNED TRANSPORTATION REVENUE	$ 428,979.72	$ 220,660.05
RESERVE FOR TRANSITION TO PEACETIME OPERATIONS	$ 2,750,000.00	$ 2,750,000.00

CAPITAL STOCK:	*Number of shares* At Dec. 31, 1945	At Dec. 31, 1944		
Prior Preferred Stock, without par value ($4.25 Cumulative Convertible):				
Authorized	None	50,000		
Issued and outstanding	None	5,387		$ 549,474.00
Preferred Stock, par value $100 per share:				
Authorized	200,000	200,000		
Issued and outstanding	None	None		
Common Stock, par value $5 per share (Note 4):				
Authorized	2,400,000	2,400,000		
Issued and outstanding	1,290,567.69	1,277,162.16	$ 6,452,838.45	$ 6,385,810.80
Reserved for option (Note 5)	50,000	None		
Employees Stock, par value $5 per share:				
Authorized	100,000	100,000		
Issued and outstanding	None	None		
SURPLUS (per attached statement):				
Paid-in surplus			$ 6,267,434.05	$ 5,855,877.70
Earned surplus			13,422,302.87	10,376,858.16
			$19,689,736.92	$16,232,735.86
COMMITMENTS (Note 6)				
			$45,857,823.39	$39,259,256.25

Explanatory notes are attached hereto.

AMERICAN AIRLINES, INC. AND CONSOLIDATED SUBSIDIARY

CONSOLIDATED STATEMENTS OF PROFIT AND LOSS

FOR THE YEARS ENDED DECEMBER 31, 1945 AND 1944

	Year ended Dec. 31, 1945	Year ended Dec. 31, 1944
OPERATING REVENUES (Note 7):		
Passenger	$37,317,430.27	$29,338,230.53
Mail	5,981,051.16	6,685,282.38
Express	2,417,104.46	2,483,245.95
Freight	967,468.14	46,676.23
Other	732,945.90	690,576.53
	$47,415,999.93	$39,244,011.62
OPERATING EXPENSES (Notes 8 and 9):		
Flying operations	$ 9,505,913.12	$ 6,849,307.32
Ground operations	6,984,296.81	5,456,997.32
Maintenance and repairs	7,326,851.53	5,344,292.40
Passenger service	3,417,190.54	2,454,383.86
Traffic and sales	4,494,019.44	3,318,115.44
Advertising and publicity	1,592,955.43	1,415,478.65
Retirement Benefit Plan and other employee welfare (Note 10)	627,557.49	658,725.04
Social security taxes	438,561.12	437,034.25
General and administrative	2,927,363.27	2,628,422.90
Provision for obsolescence and depreciation of property and equipment	1,925,182.00	1,209,793.07
	$39,239,890.75	$29,772,550.25
	$ 8,176,109.18	$ 9,471,461.37
OTHER INCOME:		
Interest, cash discounts on purchases, etc.	184,872.68	169,520.53
	$ 8,360,981.86	$ 9,640,981.90
DEDUCTIONS FROM INCOME:		
Loss on sale and retirement of property and equipment	$ 99,903.07	$ 19,031.08
Special provision for doubtful accounts receivable (U. S. Government war contracts)	—	75,000.00
Other	121,620.63	100,787.47
	$ 221,523.70	$ 194,818.55
	$ 8,139,458.16	$ 9,446,163.35
PROVISION FOR FEDERAL INCOME TAXES (Note 3)	3,800,000.00	4,050,000.00
	$ 4,339,458.16	$ 5,396,163.35
PROVISION FOR TRANSITION TO PEACETIME OPERATIONS	—	1,000,000.00
NET PROFIT CARRIED TO SURPLUS	$ 4,339,458.16	$ 4,396,163.35

Explanatory notes are attached hereto.

AMERICAN AIRLINES, INC. AND CONSOLIDATED SUBSIDIARY

CONSOLIDATED STATEMENTS OF SURPLUS

FOR THE YEARS ENDED DECEMBER 31, 1945 AND 1944

	Year ended Dec. 31, 1945	Year ended Dec. 31, 1944
PAID-IN SURPLUS		
Balance at beginning of year	$ 5,855,877.70	$ 1,942,682.50
Add:		
Arising from conversion of:		
4,692 shares of $4.25 Cumulative Convertible Preferred Stock into 13,405.53 shares of Common Stock	411,556.35	—
44,613 shares of $4.25 Cumulative Convertible Preferred Stock into 127,466.16 shares of Common Stock	—	3,913,195.20
Balance at end of year	$ 6,267,434.05	$ 5,855,877.70
EARNED SURPLUS		
Balance at beginning of year	$10,376,858.16	$ 7,411,970.86
Add: Net profit for year	4,339,458.16	4,396,163.35
	$14,716,316.32	$11,808,134.21
Deduct:		
Dividends declared:		
On Common Stock: $1.00 per share in 1945 and $1.00 per share in 1944	$ 1,290,495.00	$ 1,271,896.00
On $4.25 Cumulative Convertible Preferred Stock: $3.1875 per share in 1944	—	159,380.05
Redemption premium on 695 shares of $4.25 Cumulative Convertible Preferred Stock redeemed on January 15, 1945	3,518.45	—
	$ 1,294,013.45	$ 1,431,276.05
Balance at end of year	$13,422,302.87	$10,376,858.16

NOTES TO FINANCIAL STATEMENTS

NOTE 1:

The accompanying financial statements include in consolidation the Company's wholly-owned subsidiary, American Airlines de Mexico, S. A. The accounts of the following subsidiaries are not included in consolidation:

American Overseas Airlines, Inc.:

On July 10, 1945, the Company acquired, with the approval of the Civil Aeronautics Board, at a a cost of $3,000,000 in cash, 120,000 shares of the capital stock of American Overseas Airlines, Inc., which, upon issuance, represented 51.4% of the total number of shares outstanding. The cost of the Company's investment in this subsidiary exceeds its equity in the subsidiary's net assets, as shown by the books of the latter at December 31, 1945, by $755,493 comprised as follows:

Excess of investment over equity at date of acquisition	$828,361
Less: Equity in net profit from date of acquisition to December 31, 1945	72,868
	$755,493

The Company's equity in the net assets of this subsidiary includes $747,583 in respect of experimental and development costs deferred on the subsidiary's books. The Company has not yet adopted a policy with respect to amortization of the aforementioned excess cost at date of acquisition in the amount of $828,361 pending the adoption by the subsidiary, with the approval of the Civil Aeronautics Board, of a policy with respect to amortization of its deferred experimental and development costs.

Sky Chefs, Inc. and Airborne Instruments Laboratory, Inc.:

These subsidiaries, which are wholly-owned, are engaged respectively in airport restaurant and airline catering operations and in research and development of radio and electronic devices. The assets and operations of these subsidiaries are not material in relation to those of the Company.

The Company's equity in the net assets of Sky Chefs, Inc., as shown by the books of the latter at December 31, 1945, exceeds the Company's investment therein by $73,591 representing accumulated net profit from date of organization in 1941 to December 31, 1945. The net profit of Sky Chefs, Inc., amounted to $43,054 for the year 1945 and to $44,634 for the year 1944.

No difference exists between the Company's equity in the net assets of Airborne Instruments Laboratory, Inc. and the Company's investment therein since this subsidiary realized no profit or loss from date of organization in August, 1945, to December 31, 1945.

NOTE 2:

Land, buildings and other equipment at December 31, 1945 include approximately $683,000 (after deduction of reserve for depreciation) of such assets located in and used in airline operations within the Republic of Mexico. Net current assets in foreign countries are not substantial in amount.

NOTE 3:

No provision has been made for Federal excess profits tax for 1945 and prior years as the Company is believed to be exempt therefrom although its liability for Federal taxes on income is subject to the Internal Revenue Bureau's review of the tax returns filed or to be filed for the years 1942 through 1945.

NOTE 4:

On September 17, 1945 the Company entered into an agreement with a representative of holders of 50.75% of the common stock of Mid-Continent Airlines, Inc., subject to the approval of the Civil Aeronautics Board,

to issue one share of its common stock in exchange for each four shares of common stock of Mid-Continent Airlines, Inc., and to extend the same offer to the other stockholders of Mid-Continent Airlines, Inc. Application for approval of this agreement was filed on October 1, 1945 with the Civil Aeronautics Board which held hearings on the matter on January 21, 1946 but has not yet rendered its decision. If this acquisition is consummated, the number of shares of common stock to be issued by the Company will amount to a minimum of 49,405 shares and a maximum of 97,350 shares, depending upon the extent to which its offer is accepted by the stockholders of Mid-Continent Airlines, Inc.

All shares of the Company's common stock issued under such offer will, subject to the approval of the Civil Aeronautics Board, be recorded as issued for a consideration of $45.80 per share, being the average market price of the Company's common stock during the 18 months preceding September 17, 1945. Assuming that all stockholders of Mid-Continent Airlines, Inc., accept the Company's offer, the Company's investment therein will, subject to the approval of the Civil Aeronautics Board, be recorded on its books at $4,458,630 which is approximately $3,200,000 in excess of the net tangible assets of Mid-Continent Airlines, Inc., based on the latter's books at September 30, 1945. Such excess is considered to relate primarily to intangible asset values not carried on the books of Mid-Continent Airlines, Inc.

NOTE 5:

The Board of Directors deeming it beneficial to the Company that the Chairman of the Board have a substantial proprietary interest in the Company authorized and approved an agreement dated June 1, 1945 granting him an option to purchase 50,000 shares of the Company's authorized and unissued common stock at $58.50 per share (being $.25 per share above the quoted market closing price on the date granted). The option may be exercised or disposed of in whole or in part at any time between December 1, 1945 and June 1, 1950, date of expiration.

NOTE 6:

Commitments:

The Company has agreements with Douglas Aircraft Company, Inc., for the purchase of 50 four-engine airplanes (type DC-6), delivery thereof being scheduled to start in the latter part of 1946.

The Company is arranging to purchase from an agency of the government a total of from 50 to 55 four-engine used military airplanes and has contracted for their over-haul and conversion to passenger and to cargo airplanes. These airplanes are being currently received by the Company.

The Company has participated in the development of a high performance, twin-engined aircraft and plans to acquire 100 aircraft of that type, delivery commencing in 1947.

The Company has various commitments for the purchase of spare engines, radio equipment and spare parts in connection with the additional operating requirements resulting from the acquisition of the above mentioned airplanes.

The total cost of the above contemplated purchases and commitments, estimated at $72,750,000, together with additional commitments for the acquisition of certain major items of property and ground equipment totalling $2,250,000, will require expenditures approximated as follows:

In 1946	$42,000,000
In 1947	29,000,000
In 1948	4,000,000
	$75,000,000

On February 28, 1946 the Company borrowed from certain banks a total of $25,000,000 payable 180 days from date pursuant to unsecured promissory notes bearing interest at the rate of 1½% per annum. The Company intends to use the proceeds of such borrowings as part payment for purchases of the aforementioned equipment and facilities. The banks to which these notes were issued have agreed with the Company that at its option, upon the maturity thereof, they will accept renewal notes at the same rate in the same amount for an additional period of 180 days.

The Company has guaranteed a similar bank loan in the amount of $10,000,000 obtained on March 7, 1946 by American Overseas Airlines, Inc.

NOTE 7:

The Civil Aeronautics Board fixes the rate at which the Company is compensated for the transportation of air mail and has the authority to prescribe the fares and rates charged for the transportation of passengers, express and freight. As of January 1, 1945 the rate received by the Company for the transportation of air mail was reduced from 60¢ to 45¢ per ton mile. Reductions were made in passenger fares on March 10, 1945 and August 20, 1945 and in air express rates on January 1, 1946.

If the passenger fares in effect since August 20, 1945 had been applicable to the passenger miles flown from January 1 to August 20, 1945 and the air express rates in effect since January 1, 1946 had been applicable to the ton miles of express flown during the year 1945, the gross revenues for the year 1945 would have been reduced by approximately $1,700,000.

NOTE 8:

In the latter part of 1945 the Company granted wage and salary increases to certain groups of its employees and, effective January 1, 1946, established a forty-hour work week, with no decrease in pay for the reduction in work hours, for all employees except flight personnel and stewardesses who were already working less than forty hours per week. It is estimated that if such increases and shortened work week had been in effect since January 1, 1945 there would have been an increase of approximately $2,500,000 in salaries and wages included in operating expenses for the year 1945.

The outcome of the negotiations (now in progress with Airline Pilots Association, International; Airline Communications Employees Association; and Transport Workers Union of America, C.I.O.) cannot be anticipated at this time, but the demands upon the Company for wage and salary increases and changes in working conditions are substantial and the extent to which they are granted in final settlement may result in substantial increases in the Company's operating expenses.

NOTE 9:

Since early in 1942 services have been performed by the Company for the U. S. Government under war contracts at cost thereof and the Company has waived all profits thereon. The costs and expenses applicable to the Company's performance of such contracts are not included in the accompanying profit and loss statements, but have been charged directly to the U. S. Government. Part of the services under these contracts had been terminated at December 31, 1945 and it is expected that the remainder will be terminated by April 1, 1946. Renegotiation proceedings pursuant to the War Contracts Renegotiation Act have been concluded for 1944 and prior years, no refunds being required thereunder. The Company believes that such proceedings for the year 1945 will likewise result in no refund being required.

NOTE 10:

Under the Employees' Retirement Benefit Plan established as of December 31, 1941 the Company has made annual purchases of annuities in respect of past services rendered by employees prior to December 31, 1941. Such payments, which have been charged to profit and loss of the years in which paid, amounted to $375,000 in 1945, $375,000 in 1944 and an aggregate of $625,000 in prior years. The remaining cost of past service annuities not yet purchased at December 31, 1945 is estimated at approximately $100,000.

The cost of the Plan for services rendered since January 1, 1942 is paid currently in part by the participating employees and in part by the Company.