

CONTINENTAL AIRLINES INC /DE/
Form 10-Q
July 21, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2009

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM _____ TO _____

Commission File Number 1-10323

CONTINENTAL AIRLINES, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

74-2099724
(I.R.S. Employer
Identification No.)

1600 Smith Street, Dept. HQSEO
Houston, Texas 77002
(Address of principal executive offices)
(Zip Code)

713-324-2950

(Registrant's telephone number, including area code)

Indicate by check mark whether registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of July 20, 2009, 123,657,537 shares of Class B common stock of the registrant were outstanding.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements.

CONTINENTAL AIRLINES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions, except per share data) (Unaudited)
(2008 As Adjusted (Note 1))

	Three Months Ended June 30, 2009	Three Months Ended June 30, 2008	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
Operating Revenue:				
Passenger (excluding fees and taxes of \$379, \$408, \$725, and \$784, respectively)	\$2,767	\$3,650	\$5,384	\$6,873
Cargo	82	132	167	254
Other	277	262	536	487
	3,126	4,044	6,087	7,614
Operating Expenses:				
Aircraft fuel and related taxes	891	1,653	1,626	2,915
Wages, salaries and related costs	799	704	1,564	1,432
Aircraft rentals	235	246	472	493
Regional capacity purchase, net	217	299	431	591
Landing fees and other rentals	216	210	425	418
Maintenance, materials and repairs	161	167	314	326
Distribution costs	150	194	307	375
Depreciation and amortization	118	108	229	215
Passenger services	96	107	183	203
Special charges	44	58	48	50
Other	353	369	696	733
	3,280	4,115	6,295	7,751
Operating Loss	(154)	(71)	(208)	(137)
Nonoperating Income (Expense):				
Interest expense	(90)	(91)	(183)	(185)
Interest capitalized	8	8	17	17

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Interest income	4	16	8	40
Gain on sale of investments	-	78	-	78
Other-than-temporary impairment losses on investments	-	(29)	-	(29)
Other, net	19	40	17	39
	(59)	22	(141)	(40)
Loss before Income Taxes	(213)	(49)	(349)	(177)
Income Tax Benefit	-	44	-	90
Net Loss	\$(213)	\$ (5)	\$ (349)	\$ (87)
Basic and Diluted Loss per Share	\$(1.72)	\$(0.05)	\$(2.82)	\$(0.87)
Shares Used for Basic and Diluted Computation	124	99	124	99

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CONTINENTAL AIRLINES, INC.
CONSOLIDATED BALANCE SHEETS
(In millions, except for share data)
(2008 As Adjusted (Note 1))

ASSETS	June 30, 2009 (Unaudited)	December 31, 2008	June 30, 2008 (Unaudited)
Current Assets:			
Cash and cash equivalents	\$ 2,521	\$ 2,165	\$ 3,049
Short-term investments	247	478	358
Total unrestricted cash, cash equivalents and short-term investments	2,768	2,643	3,407
Restricted cash, cash equivalents and short-term investments	167	190	122
Accounts receivable, net	488	453	739
Spare parts and supplies, net	242	235	339
Deferred income taxes	172	216	249
Prepayments and other	494	610	602
Total current assets	4,331	4,347	5,458
Property and Equipment:			
Owned property and equipment:			
Flight equipment	8,614	8,446	7,960
Other	1,740	1,694	1,641
	10,354	10,140	9,601
Less: Accumulated depreciation	3,388	3,229	2,968
	6,966	6,911	6,633
Purchase deposits for flight equipment	257	275	328
Capital leases	194	194	190
Less: Accumulated amortization	58	53	49
	136	141	141
Total property and equipment, net	7,359	7,327	7,102
Routes and airport operating rights, net	797	804	791
Investment in student loan-related auction rate	-	-	264

securities, long-term			
Other assets, net	175	208	203
Total Assets	\$12,662	\$12,686	\$13,818

(continued on next page)

CONTINENTAL AIRLINES, INC.
CONSOLIDATED BALANCE SHEETS
(In millions, except for share data)
(2008 As Adjusted (Note 1))

LIABILITIES AND STOCKHOLDERS' EQUITY	June 30, 2009 (Unaudited)	December 31, 2008 (Unaudited)	June 30, 2008
Current Liabilities:			
Current maturities of long-term debt and capital leases	\$ 980	\$ 519	\$ 466
Accounts payable	1,062	1,021	1,043
Air traffic and frequent flyer liability	2,128	1,881	2,790
Accrued payroll	379	345	334
Accrued other liabilities	307	708	294
Total current liabilities	4,856	4,474	4,927
Long-Term Debt and Capital Leases	4,963	5,353	5,300
Deferred Income Taxes	172	216	307
Accrued Pension Liability	1,375	1,417	472
Accrued Retiree Medical Benefits	239	234	242
Other	821	869	843
C o m m i t m e n t s a n d Contingencies			
Stockholders' Equity:			
Class B common stock - \$.01 par, 400,000,000 shares authorized; 123,657,537, 123,264,534 and 109,796,597 issued	1	1	1
Additional paid-in capital	2,047	2,038	1,826
Retained earnings (accumulated deficit)	(509)	(160)	339
Accumulated other comprehensive loss	(1,303)	(1,756)	(439)
	236	123	1,727

Total stockholders'
equity

Total Liabilities and Stockholders' Equity	\$ 12,662	\$ 12,686	\$ 13,818
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The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CONTINENTAL AIRLINES, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (In millions)
 (2008 As Adjusted (Note 1))

	Six Months Ended June 30,	
	2009	2008
	(Unaudited)	
Cash Flows from Operating Activities:	\$	
Net loss	\$ (349)	\$ (87)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	229	215
Special charges	48	50
Gain on sale of investments	-	(78)
Stock-based compensation related to equity awards	3	8
Deferred income tax benefit	-	(90)
Other, net	27	26
Changes in operating assets and liabilities	401	423
Net cash provided by operating activities	359	467
Cash Flows from Investing Activities:		
Capital expenditures	(147)	(293)
Aircraft purchase deposits refunded, net	17	56
Proceeds from sales of short-term investments, net	233	82
Proceeds from sales of property and equipment	7	74
Decrease (increase) in restricted cash, cash equivalents and short-term investments	23	(21)
Proceeds from sale of Copa Holdings, S.A. stock	-	149
Proceeds from sales of investments	1	21
Other	(3)	-
Net cash provided by investing activities	131	68
Cash Flows from Financing Activities:		
Payments on long-term debt and capital lease obligations	(169)	(267)
Proceeds from issuance of long-term debt	30	483
Proceeds from public offering of common stock	-	162
Proceeds from issuance of common stock pursuant to stock plans	5	8
Net cash provided by (used in) financing activities	(134)	386
Net Increase in Cash and Cash Equivalents	356	921
Cash and Cash Equivalents - Beginning of Period	2,165	2,128

Cash and Cash Equivalents - End of Period	\$2,521	\$3,049
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Investing and Financing Activities Not Affecting Cash:

Property and equipment acquired through the issuance of debt	\$ 197	\$ 690
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The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CONTINENTAL AIRLINES, INC.
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 (Unaudited)

In our opinion, the unaudited consolidated financial statements included herein contain all adjustments necessary to present fairly our financial position, results of operations and cash flows for the periods indicated. Such adjustments, other than nonrecurring adjustments that have been separately disclosed, are of a normal, recurring nature.

The accompanying consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto for the year ended December 31, 2008 contained in our Current Report on Form 8-K dated April 24, 2009. Due to seasonal fluctuations common to the airline industry, our results of operations for the periods presented are not necessarily indicative of the results of operations to be expected for the entire year. As used in these Notes to Consolidated Financial Statements, the terms “Continental,” “we,” “us,” “our” and similar terms refer to Continental Airlines, Inc. and, unless the context indicates otherwise, its consolidated subsidiaries.

Reclassifications have been made in the prior periods’ consolidated statements of operations to conform to our new presentation for expense related to fuel and related taxes on flights operated for us by other operators under capacity purchase agreements. This expense, which is now included in aircraft fuel and related taxes, was previously reported in regional capacity purchase, net. These reclassifications do not affect operating income (loss) or net income (loss) for any period.

We have evaluated subsequent events through July 21, 2009, which is the date these financial statements were issued.

NOTE 1 – ADOPTED AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

FSP APB 14-1. On January 1, 2009, we adopted the Financial Accounting Standards Board’s (“FASB”) Staff Position No. APB 14-1, “Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)” (“FSP APB 14-1”), which clarifies the accounting for convertible debt instruments that may be settled in cash (including partial cash settlement) upon conversion. FSP APB 14-1 requires issuers to account separately for the liability and equity components of certain convertible debt instruments in a manner that reflects the issuer’s nonconvertible debt (unsecured debt) borrowing rate when interest cost is recognized. FSP APB 14-1 requires bifurcation of a component of the debt, classification of that component in equity and the accretion of the resulting discount on the debt to be recognized as part of interest expense in our consolidated statements of operations.

FSP APB 14-1 requires retrospective application to the terms of instruments as they existed for all periods presented. The adoption of FSP APB 14-1 affects the accounting for our 5% Convertible Notes issued in 2003 and due 2023 (the “5% Convertible Notes”). The retrospective application of this pronouncement affects years 2003 through 2008. Income taxes have been recorded on the foregoing adjustments to the extent tax benefits were available.

The following table sets forth the effect of the retrospective application of FSP APB 14-1 on certain previously reported line items (in millions, except per share data):

Consolidated Statements of Operations:

Three Months ended June 30, 2008		Six Months ended June 30, 2008	
Originally Reported	As Adjusted	Originally Reported	As Adjusted

Interest expense	\$(88)	\$(91)	\$(179)	\$(185)
Income tax benefit	43	44	88	90
Net loss	(3)	(5)	(83)	(87)
Basic and Diluted Loss per Share	\$(0.03)	\$(0.05)	\$(0.84)	\$(0.87)

Consolidated Balance Sheet:

	December 31, 2008		June 30, 2008	
	Originally Reported	As Adjusted	Originally Reported	As Adjusted
Long-term debt and capital leases	\$5,371	\$5,353	\$5,323	\$5,300
Deferred income tax liability	216	216	299	307
Additional paid-in capital	1,997	2,038	1,785	1,826
Retained earnings (accumulated deficit)	(137)	(160)	365	339
Total stockholders' equity	105	123	1,712	1,727

SFAS 165. In May 2009, the FASB issued Statement No. 165, "Subsequent Events" ("SFAS 165"), which establishes general standards of accounting for, and requires disclosure of, events that occur after the balance sheet date but before financial statements are issued or are available to be issued. We adopted the provisions of SFAS 165 for the quarter ended June 30, 2009. The adoption of these provisions did not have a material effect on our consolidated financial statements.

SFAS 157. In September 2006, the FASB issued Statement No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. In February 2008, the FASB issued FASB Staff Position No. FAS 157-2, "Effective Date of FASB Statement No. 157," which deferred the effective date for us to January 1, 2009 for all nonfinancial assets and liabilities, except for those that are recognized or disclosed at fair value on a recurring basis (that is, at least annually). We adopted the deferred provisions of SFAS 157 on January 1, 2009. The adoption of these provisions did not have a material effect on our consolidated financial statements.

FSP FAS 157-4. In April 2009, the FASB issued Staff Position No. 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" ("FSP FAS 157-4"), which provides additional guidance for estimating fair value in accordance with SFAS 157. We adopted the provisions of FSP FAS 157-4 for the quarter ended June 30, 2009. The adoption did not have a material effect on our consolidated financial statements.

FSP FAS 115-2. In April 2009, the FASB issued Staff Position No. FAS 115-2 and FAS 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments" ("FSP FAS 115-2"), which provides new guidance on the recognition of other-than-temporary impairments of investments in debt securities and provides new presentation and disclosure requirements for other-than-temporary impairments of investments in debt and equity securities. We adopted the provisions of FSP FAS 115-2 for the quarter ended June 30, 2009. The adoption did not have a material effect on our consolidated financial statements.

FSP FAS 107-1 and ABP 28-1. In April 2009, the FASB issued Staff Position No. FAS 107-1 and APB 28-1, "Interim Disclosures about Fair Value of Financial Instruments" ("FSP FAS 107-1"). FSP FAS 107-1 amends SFAS No. 107, "Disclosures about Fair Value of Financial Instruments" ("SFAS 107") to require disclosures about fair value of financial

instruments in interim reporting periods. Such disclosures were previously required only in annual financial statements. We adopted the provisions of FSP FAS 107-1 for the quarter ended June 30, 2009. Because FSP FAS 107-1 applies only to financial statement disclosures, the adoption did not have a material effect on our consolidated financial statements.

FSP FAS 132(R)-1. In December 2008, the FASB affirmed Staff Position No. FAS 132(R)-1, "Employers' Disclosures about Postretirement Benefit Plan Assets" ("FSP FAS 132(R)-1"). FSP FAS 132(R)-1 requires additional disclosures about assets held in an employer's defined benefit pension or other postretirement plan, primarily related to categories and fair value measurements of plan assets. FSP FAS 132(R)-1 is effective for us as of December 31, 2009. Because FSP FAS 132(R)-1 applies only to financial statement disclosures, the adoption is not expected to have a material effect on our consolidated financial statements.

NOTE 2 - LOSS PER SHARE

Because we incurred a net loss in the three and six months ended June 30, 2009 and 2008, basic and diluted loss per share for each period were calculated as our net loss divided by the weighted average shares outstanding. Approximately 13 million potential shares of our common stock related to convertible debt securities were excluded from the computation of diluted loss per share for the three and six months ended June 30, 2009 and 2008 because they were antidilutive. In addition, approximately 8 million weighted average options to purchase shares of our common stock were excluded from the computation of diluted loss per share for each of the three and six months ended June 30, 2009 and 2008 because the effect of including the options would have been antidilutive.

NOTE 3 - FLEET INFORMATION

As of June 30, 2009, our operating fleet consisted of 351 mainline jets and 266 regional aircraft. The 351 mainline jets are operated exclusively by us, while the 266 regional aircraft are operated on our behalf by other operators under capacity purchase agreements.

We own or lease 274 regional jets. Of these, 214 are leased or subleased to ExpressJet Airlines, Inc. ("ExpressJet") and operated on our behalf under a capacity purchase agreement with ExpressJet, 30 are subleased to ExpressJet and are not operated on our behalf and 30 ERJ-135 regional jet aircraft are temporarily grounded. Additionally, our regional operating fleet includes 52 regional jet and turboprop aircraft owned or leased by third parties that are operated on our behalf by other operators under capacity purchase agreements.

The following table summarizes our operating fleet (aircraft operated by us and by others on our behalf) as of June 30, 2009:

Aircraft Type	Total	Owned	Leased	Third-Party Aircraft
Mainline (a):				
777-200ER	20	8	12	-
767-400ER	16	14	2	-
767-200ER	10	9	1	-
757-300	17	9	8	-
757-200	41	15	26	-
737-900ER	22	22	-	-
737-900	12	8	4	-
737-800	117	44	73	-
737-700	36	12	24	-
737-500	40	-	40	-
737-300	20	12	8	-
Total mainline	351	153		