

ATLAS AIR WORLDWIDE HOLDINGS INC

Form 10-Q

July 30, 2015

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, DC 20549**

**FORM 10-Q**

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

**For the quarterly period ended June 30, 2015**

**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: 001-16545**

**Atlas Air Worldwide Holdings, Inc.**

**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
  
**incorporation)**

**13-4146982**  
**(IRS Employer**  
  
**Identification No.)**

**2000 Westchester Avenue, Purchase, New York**  
**(Address of principal executive offices)**

**10577**  
**(Zip Code)**

**(914) 701-8000**

**(Registrant's telephone number, including area code)**

**Not Applicable**

**(Former name, former address and former fiscal year, if changed since last report)**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  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 (§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 definitions of accelerated filer, large 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

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 27, 2015, there were 25,052,851 shares of the registrant's Common Stock outstanding.



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Table of Contents**PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****Atlas Air Worldwide Holdings, Inc.****Consolidated Balance Sheets***(in thousands, except share data)**(Unaudited)*

	<b>June 30, 2015</b>	<b>December 31, 2014</b>
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 514,750	\$ 298,601
Short-term investments	24,373	17,802
Restricted cash	15,731	14,281
Accounts receivable, net of allowance of \$1,631 and \$1,658, respectively	152,906	162,092
Prepaid maintenance	15,589	20,806
Deferred taxes	41,862	40,923
Prepaid expenses and other current assets	31,313	51,599
Total current assets	796,524	606,104
<b>Property and Equipment</b>		
Flight equipment	3,489,587	3,448,791
Ground equipment	55,227	51,418
Less: accumulated depreciation	(400,368)	(348,036)
Purchase deposits for flight equipment	58,820	20,054
Property and equipment, net	3,203,266	3,172,227
<b>Other Assets</b>		
Long-term investments and accrued interest	106,951	120,478
Deposits and other assets	77,337	80,258
Intangible assets, net	62,918	67,410
<b>Total Assets</b>	<b>\$ 4,246,996</b>	<b>\$ 4,046,477</b>
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 39,274	\$ 42,864
Accrued liabilities	261,342	251,594
Current portion of long-term debt	180,902	181,202
Total current liabilities	481,518	475,660

**Other Liabilities**

Long-term debt	1,812,483	1,736,739
Deferred taxes	370,216	350,868
Other liabilities	67,442	65,415

Total other liabilities	2,250,141	2,153,022
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**Commitments and contingencies****Equity**

## Stockholders' Equity

Preferred stock, \$1 par value; 10,000,000 shares authorized; no shares issued

Common stock, \$0.01 par value; 50,000,000 shares authorized; 28,938,970 and 28,561,160 shares issued, 25,050,599 and 24,807,718, shares outstanding (net of treasury stock), as of June 30, 2015 and December 31, 2014, respectively

	289	286
Additional paid-in-capital	618,911	573,133
Treasury stock, at cost; 3,888,371 and 3,753,442 shares, respectively	(151,636)	(145,322)
Accumulated other comprehensive loss	(9,119)	(9,572)
Retained earnings	1,056,892	999,270

Total equity	1,515,337	1,417,795
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<b>Total Liabilities and Equity</b>	<b>\$ 4,246,996</b>	<b>\$ 4,046,477</b>
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*See accompanying Notes to Unaudited Consolidated Financial Statements*

**Table of Contents****Atlas Air Worldwide Holdings, Inc.****Consolidated Statements of Operations***(in thousands, except per share data)**(Unaudited)*

	<b>For the Three Months Ended</b>		<b>For the Six Months Ended</b>	
	<b>June 30, 2015</b>	<b>June 30, 2014</b>	<b>June 30, 2015</b>	<b>June 30, 2014</b>
<b>Operating Revenue</b>				
ACMI	\$ 189,255	\$ 186,720	\$ 378,302	\$ 384,861
Charter	235,436	225,234	455,574	402,607
Dry leasing	27,401	25,524	59,320	50,200
Other	3,741	3,691	7,482	6,864
<b>Total Operating Revenue</b>	<b>455,833</b>	<b>441,169</b>	<b>900,678</b>	<b>844,532</b>
<b>Operating Expenses</b>				
Salaries, wages and benefits	86,862	77,948	175,635	150,803
Aircraft fuel	96,711	103,842	174,826	185,586
Maintenance, materials and repairs	41,438	50,386	100,270	109,432
Aircraft rent	36,811	34,826	71,072	70,236
Depreciation and amortization	31,936	30,381	63,966	58,536
Navigation fees, landing fees and other rent	22,666	30,906	46,169	58,032
Travel	23,830	18,774	44,643	36,056
Passenger and ground handling services	21,353	21,859	41,316	41,230
Loss on disposal of aircraft	114	14,679	1,323	14,679
Special charge	499	1,449	(69)	9,477
Other	32,329	29,462	63,273	55,678
<b>Total Operating Expenses</b>	<b>394,549</b>	<b>414,512</b>	<b>782,424</b>	<b>789,745</b>
<b>Operating Income</b>	<b>61,284</b>	<b>26,657</b>	<b>118,254</b>	<b>54,787</b>
<b>Non-operating Expenses (Income)</b>				
Interest income	(4,425)	(4,719)	(8,913)	(9,446)
Interest expense	25,033	26,365	49,581	52,817
Capitalized interest	(177)	(67)	(203)	(379)
Other expense (income), net	(284)	(88)	391	64
<b>Total Non-operating Expenses (Income)</b>	<b>20,147</b>	<b>21,491</b>	<b>40,856</b>	<b>43,056</b>
<b>Income before income taxes</b>	<b>41,137</b>	<b>5,166</b>	<b>77,398</b>	<b>11,731</b>
<b>Income tax expense</b>	<b>12,747</b>	<b>(23,815)</b>	<b>19,776</b>	<b>(21,276)</b>

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<b>Net Income</b>	28,390	28,981	57,622	33,007
Less: Net income (loss) attributable to noncontrolling interests		(612)		(4,530)
<b>Net Income Attributable to Common Stockholders</b>	\$ 28,390	\$ 29,593	\$ 57,622	\$ 37,537
<b>Earnings per share:</b>				
Basic	\$ 1.13	\$ 1.17	\$ 2.31	\$ 1.49
Diluted	\$ 1.13	\$ 1.17	\$ 2.29	\$ 1.49
<b>Weighted average shares:</b>				
Basic	25,029	25,241	24,953	25,169
Diluted	25,198	25,279	25,135	25,215

*See accompanying Notes to Unaudited Consolidated Financial Statements*



**Table of Contents****Atlas Air Worldwide Holdings, Inc.****Consolidated Statements of Comprehensive Income***(in thousands)**(Unaudited)*

	<b>For the Three Months Ended</b>		<b>For the Six Months Ended</b>	
	<b>June 30, 2015</b>	<b>June 30, 2014</b>	<b>June 30, 2015</b>	<b>June 30, 2014</b>
<b>Net Income</b>	\$ 28,390	\$ 28,981	\$ 57,622	\$ 33,007
<b>Other comprehensive income (loss):</b>				
Interest rate derivatives:				
Net change in fair value				(251)
Reclassification to interest expense	638	682	1,288	1,372
Income tax expense	(244)	(261)	(492)	(506)
Foreign currency translation:				
Translation adjustment	(285)	191	(343)	349
<b>Other comprehensive income</b>	<b>109</b>	<b>612</b>	<b>453</b>	<b>964</b>
<b>Comprehensive Income</b>	<b>28,499</b>	<b>29,593</b>	<b>58,075</b>	<b>33,971</b>
Less: Comprehensive income (loss) attributable to noncontrolling interests		(515)		(4,352)
<b>Comprehensive Income Attributable to Common Stockholders</b>	<b>\$ 28,499</b>	<b>\$ 30,108</b>	<b>\$ 58,075</b>	<b>\$ 38,323</b>

*See accompanying Notes to Unaudited Consolidated Financial Statements*

**Table of Contents****Atlas Air Worldwide Holdings, Inc.****Consolidated Statements of Cash Flows***(in thousands)**(Unaudited)*

	<b>For the Six Months Ended</b>	
	<b>June 30, 2015</b>	<b>June 30, 2014</b>
<b>Operating Activities:</b>		
Net Income	\$ 57,622	\$ 33,007
Adjustments to reconcile Net Income to net cash provided by operating activities:		
Depreciation and amortization	73,263	67,195
Accretion of debt securities discount	(3,760)	(4,081)
Provision for allowance for doubtful accounts	46	232
Special charge, net of cash payments	(715)	7,171
Loss on disposal of aircraft	1,323	14,679
Deferred taxes	19,773	(21,498)
Stock-based compensation expense	9,837	5,805
Changes in:		
Accounts receivable	10,135	(23,248)
Prepaid expenses and other current assets	8,937	27,613
Deposits and other assets	1,645	(4,603)
Accounts payable and accrued liabilities	(7,009)	4,854
Net cash provided by operating activities	171,097	107,126
<b>Investing Activities:</b>		
Capital expenditures	(22,117)	(10,653)
Purchase deposits and payments for flight equipment	(62,841)	(494,072)
Changes in restricted cash	(1,450)	(6,724)
Proceeds from short-term investments	2,394	2,060
Proceeds from disposal of aircraft	24,625	
Net cash used for investing activities	(59,389)	(509,389)
<b>Financing Activities:</b>		
Proceeds from debt issuance	224,500	572,552
Customer maintenance reserves received	8,701	8,757
Customer maintenance reserves paid	(1,752)	
Proceeds from sale of warrants	36,290	
Payments for convertible note hedges	(52,903)	
Proceeds from stock option exercises	1,193	
Purchase of treasury stock	(6,314)	(4,377)
Excess tax benefit from stock-based compensation expense	588	(1,973)
Payment of debt issuance costs	(6,812)	(17,087)

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Payments of debt	(99,050)	(201,021)
Net cash provided by financing activities	104,441	356,851
Net increase (decrease) in cash and cash equivalents	216,149	(45,412)
Cash and cash equivalents at the beginning of period	298,601	321,816
Cash and cash equivalents at the end of period	\$ 514,750	\$ 276,404
<b>Non-cash Investing and Financing Activities:</b>		
Acquisition of flight equipment included in Accounts payable and accrued liabilities	\$ 6,940	\$ 29,087
Disposition of aircraft included in Accounts receivable	\$	\$ 7,000

*See accompanying Notes to Unaudited Consolidated Financial Statements*

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## Atlas Air Worldwide Holdings, Inc.

## Consolidated Statements of Stockholders' Equity

*(in thousands, except share data)**(Unaudited)*

	Common Stock	Treasury Stock	Accumulated Additional Paid-In Capital	Other Comprehensive Loss	Retained Earnings	Total Stockholders' Equity	Noncontrolling Interest	Total Equity
<b>Balance at December 31, 2013</b>	\$ 282	\$ (125,826)	\$ 561,481	\$ (10,677)	\$ 892,513	\$ 1,317,773	\$ 4,352	\$ 1,322,125
Net Income (loss)					37,537	37,537	(4,530)	33,007
Other comprehensive income (loss)				786		786	178	964
Stock option and restricted stock compensation			5,805			5,805		5,805
Purchase of 129,430 shares of treasury stock		(4,377)				(4,377)		(4,377)
Issuance of 346,925 shares of restricted stock	3		(3)					
Tax benefit (expense) on restricted stock and stock options			(1,973)			(1,973)		(1,973)
<b>Balance at June 30, 2014</b>	\$ 285	\$ (130,203)	\$ 565,310	\$ (9,891)	\$ 930,050	\$ 1,355,551	\$	\$ 1,355,551

	Common Stock	Treasury Stock	Accumulated Additional Paid-In Capital	Other Comprehensive Loss	Retained Earnings	Total Stockholders' Equity	Noncontrolling Interest	Total Equity
<b>Balance at December 31, 2014</b>	\$ 286	\$ (145,322)	\$ 573,133	\$ (9,572)	\$ 999,270	\$ 1,417,795	\$	\$ 1,417,795
Net Income (loss)					57,622	57,622		57,622
Other comprehensive income (loss)				453		453		453
Stock option and restricted stock compensation			9,837			9,837		9,837

Purchase of 134,929 shares of treasury stock		(6,314)		(6,314)		(6,314)
Exercise of 25,373 employee stock options		1,193		1,193		1,193
Issuance of 352,437 shares of restricted stock	3	(3)				
Equity component of convertible notes, net of tax		32,233		32,233		32,233
Purchase of convertible note hedges, net of tax		(33,837)		(33,837)		(33,837)
Issuance of warrants		36,290		36,290		36,290
Tax benefit (expense) on restricted stock and stock options		65		65		65
<b>Balance at June 30, 2015</b>	\$ 289	\$ (151,636)	\$ 618,911	\$ (9,119)	\$ 1,056,892	\$ 1,515,337

*See accompanying Notes to Unaudited Consolidated Financial Statements*

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**Atlas Air Worldwide Holdings, Inc.**

**Notes to Unaudited Consolidated Financial Statements**

**June 30, 2015**

**1. Basis of Presentation**

Our consolidated financial statements include the accounts of the holding company, Atlas Air Worldwide Holdings, Inc. ( AAWW ) and its consolidated subsidiaries. AAWW is the parent company of its principal operating subsidiary, Atlas Air, Inc. ( Atlas ), and of Polar Air Cargo LLC ( Old Polar ). AAWW is also the parent company of several subsidiaries related to our dry leasing services (collectively referred to as Titan ).

The terms we, us, our, and the Company mean AAWW and all entities included in its consolidated financial statements.

We provide outsourced aircraft and aviation operating services throughout the world, serving Africa, Asia, Australia, Europe, the Middle East, North America and South America through: (i) contractual service arrangements, including those through which we provide aircraft to customers and value-added services, including crew, maintenance and insurance ( ACMI ), as well as those through which we provide crew, maintenance and insurance, with the customer providing the aircraft ( CMI ); (ii) cargo and passenger charter services ( Charter ); and (iii) dry leasing aircraft and engines ( Dry Leasing or Dry Lease ).

The accompanying unaudited consolidated financial statements and related notes (the Financial Statements ) have been prepared in accordance with the U.S. Securities and Exchange Commission (the SEC ) requirements for quarterly reports on Form 10-Q, and consequently exclude certain disclosures normally included in audited consolidated financial statements prepared in conformity with accounting principles generally accepted in the United States of America ( GAAP ). All significant intercompany accounts and transactions have been eliminated. The Financial Statements should be read in conjunction with the audited consolidated financial statements and the notes included in the AAWW Annual Report on Form 10-K for the year ended December 31, 2014, which includes additional disclosures and a summary of our significant accounting policies. The December 31, 2014 balance sheet data was derived from that Annual Report. In our opinion, the Financial Statements contain all adjustments, consisting of normal recurring items, necessary to fairly state the financial position of AAWW and its consolidated subsidiaries as of June 30, 2015, the results of operations for the three and six months ended June 30, 2015 and 2014, comprehensive income for the three and six months ended June 30, 2015 and 2014, cash flows for the six months ended June 30, 2015 and 2014, and shareholders equity as of and for the six months ended June 30, 2015 and 2014.

Our quarterly results are subject to seasonal and other fluctuations, and the operating results for any quarter are therefore not necessarily indicative of results that may be otherwise expected for the entire year.

Except for per share data, all dollar amounts are in thousands unless otherwise noted.

Certain reclassifications have been made to prior periods consolidated financial statement amounts and related note disclosures to conform to the current year s presentation, including the presentation of segments.

**2. Recent Accounting Pronouncements**

In May 2014, the Financial Accounting Standards Board ( FASB ) amended its accounting guidance for revenue recognition. The fundamental principles of the new guidance are that companies should recognize revenue in a manner that reflects the timing of the transfer of services to customers and consideration that a company expects to receive for the services provided. It also requires additional disclosures necessary for the financial statement users to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. In July 2015, the FASB voted to defer the effective date by one year to the beginning of 2018 and permit early adoption of the standard, but not before the beginning of 2017. We are currently assessing the impact the amended guidance will have on our financial statements.

In April 2015, the FASB amended its guidance for presenting debt issuance costs. The new guidance requires debt issuance costs to be presented in the balance sheet as a reduction of the carrying amount of the related debt liability instead of as an asset. We early adopted this guidance retrospectively effective March 31, 2015 and its adoption did not have a material impact on our financial condition, results of operations or cash flows. The amount of debt issuance costs classified on our balance sheet as a reduction of debt was \$55.6 million at June 30, 2015 and \$55.1 million at December 31, 2014.

**Table of Contents****3. Related Parties*****DHL Investment and Polar***

AAWW has a 51% equity interest and 75% voting interest in Polar Air Cargo Worldwide, Inc. ( Polar ). DHL Network Operations (USA), Inc. ( DHL ), a subsidiary of Deutsche Post AG ( DP ), holds a 49% equity interest and a 25% voting interest in Polar. Polar is a variable interest entity that we do not consolidate because we are not the primary beneficiary as the risks associated with the direct costs of operation are with DHL. We record our share of Polar's results under the equity method of accounting. Under a 20-year blocked space agreement (the BSA ), Polar provides air cargo capacity to DHL. Atlas has several agreements with Polar to provide ACMI, CMI, administrative, sales and ground support services to one another. We do not have any financial exposure to fund debt obligations or operating losses of Polar, except for any liquidated damages that we could incur under these agreements. The following table summarizes our transactions with Polar:

	For the Three Months Ended		For the Six Months Ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
<b>Revenue and Expenses:</b>				
ACMI segment revenue from Polar	\$ 94,105	\$ 74,144	\$ 185,518	\$ 143,839
Other revenue from Polar	\$ 2,842	\$ 2,842	\$ 5,687	\$ 5,684
Ground handling and airport fees paid to Polar	\$ 436	\$ 448	\$ 1,227	\$ 772

	June 30, 2015	December 31, 2014
<b>Accounts receivable/payable as of:</b>		
Receivables from Polar	\$ 6,526	\$ 5,702
Payables to Polar	\$ 641	\$ 2,611

	June 30, 2015	December 31, 2014
<b>Aggregate Carrying Value of Polar Investment as of:</b>		
	\$ 4,870	\$ 4,870

***GATS***

We hold a 50% interest in GATS GP (BVI) Ltd. ( GATS ), a joint venture with an unrelated third party. The purpose of the joint venture is to purchase rotatable parts and provide repair services for those parts, primarily for our 747-8F aircraft. The joint venture is a variable interest entity that we do not consolidate because we are not the primary beneficiary as we do not exercise financial control. As of June 30, 2015 and December 31, 2014, our investment in GATS was \$18.8 million and \$16.4 million, respectively, and our maximum exposure to losses from the entity is limited to our investment, which is comprised primarily of rotatable inventory parts. GATS does not have any third-party debt obligations. We had Accounts payable to GATS of \$1.7 million as of June 30, 2015 and \$1.5 million as of December 31, 2014.

**4. Special Charge**



During the three and six months ended June 30, 2014, we recognized \$1.6 million and \$3.9 million, respectively, of employee termination benefits related to British Airways Plc's (British Airways) return of three 747-8F aircraft in 2014. In addition, we recognized a reserve of \$5.2 million during the six months ended June 30, 2014 related to a loan from Global Supply Systems Limited (GSS), a consolidated subsidiary, to its then 51% U.K. shareholder.

A summary of the Special charge liabilities is as follows:

	<b>Lease Termination Costs</b>	<b>GSS Employee Termination Benefits</b>	<b>Other</b>	<b>Total</b>
Liability as of December 31, 2014	\$ 2,437	\$ 1,014	\$ 100	\$ 3,551
Special charge items, net	(532)	35	14	(483)
Cash payments	(1,817)	(1,049)	(114)	(2,980)
Liability as of June 30, 2015	\$ 88	\$	\$	\$ 88

Substantially all remaining cash payments related to Special charge liabilities are expected to be paid in 2015.

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Accrued liabilities consisted of the following as of:

	<b>June 30, 2015</b>	<b>December 31, 2014</b>
Customer maintenance reserves	\$ 65,042	\$ 64,756
Maintenance	45,544	50,702
Aircraft fuel	37,262	15,078
Salaries, wages and benefits	37,122	48,548
Deferred revenue	13,406	10,705
Other	62,966	61,805
<b>Accrued liabilities</b>	<b>\$ 261,342</b>	<b>\$ 251,594</b>

**6. Debt*****Convertible Notes***

In June 2015, we issued \$224.5 million aggregate principal amount of convertible senior notes (the *Convertible Notes*) in an underwritten public offering. The *Convertible Notes* are senior unsecured obligations and accrue interest payable semi-annually on June 1 and December 1 of each year at an annual rate of 2.25%. The *Convertible Notes* will mature on June 1, 2022, unless earlier converted or repurchased pursuant to their terms.

We used a portion of the net proceeds in June 2015 to fund the cost of the convertible note hedge transactions, described below, and in July 2015 to refinance higher-rate equipment notes funded by Enhanced Equipment Trust Certificates (*EETCs*) related to three 747-400 freighter aircraft. We expect to use a portion of the net proceeds during the third quarter of 2015 to refinance additional higher-rate *EETCs* for two 747-400 freighter aircraft, for which we issued a notice of redemption in July 2015. In addition, we expect to use a portion of the net proceeds for working capital and capital expenditures, for repayment or refinancing of debt, and for general corporate purposes.

Each \$1,000 of principal of the *Convertible Notes* will initially be convertible into 13.5036 shares of our common stock, which is equal to an initial conversion price of \$74.05 per share. The conversion rate will be subject to adjustment upon the occurrence of certain specified events but will not be adjusted for accrued and unpaid interest, except in certain limited circumstances. Upon the occurrence of a *make-whole fundamental change*, we will, in certain circumstances, increase the conversion rate by a number of additional shares of our common stock for *Convertible Notes* converted in connection with such *make-whole fundamental change*. Additionally, if we undergo a *fundamental change*, a holder will have the option to require us to repurchase all or a portion of its *Convertible Notes* for cash at a price equal to 100% of the principal amount of the *Convertible Notes* being repurchased plus any accrued and unpaid interest through, but excluding, the *fundamental change repurchase date*.

In connection with the offering of the *Convertible Notes*, we entered into convertible note hedge transactions whereby we have the option to purchase initially (subject to adjustment for certain specified events) a total of 3,031,558 shares of our common stock at a price of \$74.05 per share. The total cost of the convertible note hedge transactions was \$52.9 million. In addition, we sold warrants to the option counterparties whereby the holders of the warrants have the option to purchase initially (subject to adjustment for certain specified events) a total of 3,031,558 shares of our common stock at a price of \$95.01. We received \$36.3 million in cash proceeds from the sale of these warrants.

Taken together, the purchase of the convertible note hedges and the sale of warrants are intended to offset any actual dilution from the conversion of the Convertible Notes and to effectively increase the overall conversion price from \$74.05 to \$95.01 per share. The \$16.6 million net cost incurred in connection with the convertible note hedges and warrants was recorded as a reduction to additional paid-in capital, net of tax, in the consolidated balance sheet as of June 30, 2015.

On or after September 1, 2021 until the close of business on the second scheduled trading day immediately preceding the maturity date, a holder may convert all or a portion of its Convertible Notes.

Upon conversion, the Convertible Notes will be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock. Our current intent and policy is to settle conversions with a combination of cash and shares of common stock with the principal amount of the Convertible Notes paid in cash.

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Holders may convert their Convertible Notes at their option at any time prior to September 1, 2021, only under the following circumstances:

during any calendar quarter (and only during such calendar quarter) commencing after September 30, 2015 if, for each of at least 20 trading days (whether or not consecutive) during the 30 consecutive trading day period ending on, and including, the last trading day of the immediately preceding calendar quarter, the last reported sale price of our common stock for such trading day is equal to or greater than 130% of the conversion price on such trading day;

during the five consecutive business day period immediately following any five consecutive trading day period (the measurement period) in which, for each trading day of the measurement period, the trading price per \$1,000 principal amount of the Convertible Notes for such trading day was less than 98% of the product of the last reported sale price of our common stock for such trading day and the conversion rate on such trading day; or

upon the occurrence of specified corporate events.

We separately account for the liability and equity components of the Convertible Notes. The carrying amount of the liability component was determined by measuring the fair value of a similar liability that does not have an associated conversion feature, assuming our non-convertible unsecured debt borrowing rate. The carrying value of the equity component, the conversion option, which is recognized as additional paid-in-capital, net of tax, creates a debt discount on the Convertible Notes. The debt discount was determined by deducting the relative fair value of the liability component from the proceeds of the Convertible Notes and is amortized to interest expense using an effective interest rate of 6.44% over the term of the Convertible Notes. As of June 30, 2015, the remaining life of the Convertible Notes is 6.9 years. The equity component will not be remeasured as long as it continues to meet the conditions for equity classification.

As of June 30, 2015, the Convertible Notes consisted of the following:

Liability component:	
Proceeds	\$ 224,500
Less: debt discount, net of amortization	(52,436)
Less: debt issuance cost, net of amortization	(5,156)
Net carrying amount	\$ 166,908
Equity component (1)	\$ 52,903

(1) Included in Additional paid-in capital on the consolidated balance sheet as of June 30, 2015.

The debt issuance costs related to the issuance of the Convertible Notes were allocated to the liability and equity components based on their relative values, as determined above. Total debt issuance costs were \$6.8 million, of which

\$5.2 million was allocated to the liability component and \$1.6 million was allocated to the equity component. The debt issuance costs allocated to the liability component are amortized to interest expense using the effective interest method over the term of the Convertible Notes.

The following table presents the amount of interest expense recognized related to the Convertible Notes:

	<b>For the Three and Six Months Ended June 30, 2015</b>	
Contractual interest coupon	\$	393
Amortization of debt discount		467
Amortization of debt issuance costs		51
Total interest expense recognized	\$	911

## 7. Income Taxes

Our effective income tax rates were an expense of 31.0% for the three months ended June 30, 2015 and a benefit of 461.0% for the three months ended June 30, 2014. Our effective income tax rates were an expense of 25.6% for the six

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months ended June 30, 2015 and a benefit of 181.4% for the six months ended June 30, 2014. The effective rate for the six months ended June 30, 2015 differed from the U.S. federal statutory rate primarily due to an income tax benefit of \$4.0 million, net of reserves, related to extraterritorial income from leasing certain of our aircraft ( ETI ). The effective rate for the three and six months ended June 30, 2014 differed from the U.S. federal statutory rate primarily due to an income tax benefit of \$24.0 million, net of reserves, related to ETI, partially offset by losses associated with GSS for which we have recognized a valuation allowance due to the uncertainty that the benefit of the losses will be realized. The effective rates also differed from the U.S. federal statutory rate due to the income tax impact of foreign operations taxed at different rates, our assertion to indefinitely reinvest the net earnings of certain foreign subsidiaries outside the U.S., U.S. state income taxes, the nondeductibility of certain expenses for tax purposes, adjustments to our liability for uncertain tax positions, and the relationship of these items to our projected operating results for the year. For interim accounting purposes, we recognize income taxes using an estimated annual effective tax rate.

As a result of current and expected future growth in our Dry Leasing business, we determined to indefinitely reinvest the net earnings of certain foreign subsidiaries engaged in this business outside of the U.S. Our effective income tax rates for the three and six months ended June 30, 2015 and 2014 were favorably impacted by this determination. As of June 30, 2015, our undistributed net earnings of foreign subsidiaries for which deferred taxes have not been provided were \$63.1 million, and the unrecognized deferred tax liability associated with these earnings was \$22.1 million.

**8. Financial Instruments**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). Inputs used to measure fair value are classified in the following hierarchy:

- Level 1      Unadjusted quoted prices in active markets for identical assets or liabilities;
  - Level 2      Other inputs that are observable directly or indirectly, such as quoted prices in active markets for similar assets or liabilities, or inactive quoted prices for identical assets or liabilities in inactive markets;
  - Level 3      Unobservable inputs reflecting assumptions about the inputs used in pricing the asset or liability.
- We endeavor to utilize the best available information to measure fair value.

The carrying value of Cash and cash equivalents, Short-term investments and Restricted cash is based on cost, which approximates fair value.

Long-term investments consist of debt securities for which we have both the ability and the intent to hold until maturity. These investments are classified as held-to-maturity and reported at amortized cost. The fair value of our Long-term investments is based on a discounted cash flow analysis using the contractual cash flows of the investments and a discount rate derived from unadjusted quoted interest rates for debt securities of comparable risk. Such debt securities represent investments in Pass-Through Trust Certificates related to EETCs issued by Atlas in 1998, 1999 and 2000.

The fair value of our term loans, notes guaranteed by the Export-Import Bank of the United States ( Ex-Im Bank ) and EETCs are based on a discounted cash flow analysis using current borrowing rates for instruments with similar terms.

The fair value of our Convertible Notes is based on unadjusted quoted market prices for these securities.



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The following table summarizes the carrying amount, estimated fair value and classification of our financial instruments as of:

	<b>June 30, 2015</b>				
	<b>Carrying Value</b>	<b>Fair Value</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
<b>Assets</b>					
Cash and cash equivalents	\$ 514,750	\$ 514,750	\$ 514,750	\$	\$
Short-term investments	24,373	24,373			24,373
Restricted cash	15,731	15,731	15,731		
Long-term investments and accrued interest	106,951	142,799			142,799
	\$ 661,805	\$ 697,653	\$ 530,481	\$	\$ 167,172
<b>Liabilities</b>					
Term loans	\$ 910,383	\$ 945,633	\$	\$	\$ 945,633
Ex-Im Bank guaranteed notes	725,320	752,443			752,443
EETCs	190,774	243,436			243,436
Convertible Notes	166,908	221,454	221,454		
	\$ 1,993,385	\$ 2,162,966	\$ 221,454	\$	\$ 1,941,512

	<b>December 31, 2014</b>				
	<b>Carrying Value</b>	<b>Fair Value</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
<b>Assets</b>					
Cash and cash equivalents	\$ 298,601	\$ 298,601	\$ 298,601	\$	\$
Short-term investments	17,802	17,802			17,802
Restricted cash	14,281	14,281	14,281		
Long-term investments and accrued interest	120,478	154,743			154,743
	\$ 451,162	485,427	312,882		172,545
<b>Liabilities</b>					
Term loans	\$ 945,813	\$ 982,036	\$	\$	\$ 982,036
Ex-Im Bank guaranteed notes	760,389	789,834			789,834
EETCs	211,739	270,333			270,333
	\$ 1,917,941	\$ 2,042,203	\$	\$	\$ 2,042,203

The following table presents the carrying value, gross unrealized gain (loss) and fair value of our long-term investments and accrued interest by contractual maturity as of:

**June 30, 2015****December 31, 2014**



	<b>Carrying Value</b>	<b>Gross Unrealized Gain (Loss)</b>	<b>Fair Value</b>	<b>Carrying Value</b>	<b>Gross Unrealized Gain (Loss)</b>	<b>Fair Value</b>
<b>Debt securities</b>						
Due after one but within five years	\$ 72,277	\$ 1,776	\$ 74,053	\$ 40,040	\$ 9,700	\$ 49,740
Due after five but within ten years	34,674	34,072	68,746	80,438	24,565	105,003
<b>Total</b>	<b>\$ 106,951</b>	<b>\$ 35,848</b>	<b>\$ 142,799</b>	<b>\$ 120,478</b>	<b>\$ 34,265</b>	<b>\$ 154,743</b>

## 9. Segment Reporting

We currently have the following three reportable segments: ACMI, Charter and Dry Leasing. We use an economic performance metric ( Direct Contribution ) that shows the profitability of each segment after allocation of operating and

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ownership costs. The following table sets forth Operating Revenue and Direct Contribution for our reportable segments reconciled to Operating Income and Income before Income Taxes:

	For the Three Months Ended		For the Six Months Ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
<b>Operating Revenue:</b>				
ACMI	\$ 189,255	\$ 186,720	\$ 378,302	\$ 384,861
Charter	235,436	225,234	455,574	402,607
Dry Leasing	27,401	25,524	59,320	50,200
Other	3,741	3,691	7,482	6,864
<b>Total Operating Revenue</b>	<b>\$ 455,833</b>	<b>\$ 441,169</b>	<b>\$ 900,678</b>	<b>\$ 844,532</b>
<b>Direct Contribution:</b>				
ACMI	\$ 51,157	\$ 44,677	\$ 91,059	\$ 90,133
Charter	25,019	8,196	55,478	4,007
Dry Leasing	10,894	8,738	26,419	16,909
<b>Total Direct Contribution for Reportable Segments</b>	<b>87,070</b>	<b>61,611</b>	<b>172,956</b>	<b>111,049</b>
Add back (subtract):				
Unallocated income and expenses, net*	(45,320)	(40,317)	(94,304)	(75,162)
Special charge	(499)	(1,449)	69	(9,477)
Loss on disposal of aircraft	(114)	(14,679)	(1,323)	(14,679)
<b>Income before Income Taxes</b>	<b>41,137</b>	<b>5,166</b>	<b>77,398</b>	<b>11,731</b>
Add back (subtract):				
Interest income	(4,425)	(4,719)	(8,913)	(9,446)
Interest expense	25,033	26,365	49,581	52,817
Capitalized interest	(177)	(67)	(203)	(379)
Other expense (income), net	(284)	(88)	391	64
<b>Operating Income</b>	<b>\$ 61,284</b>	<b>\$ 26,657</b>	<b>\$ 118,254</b>	<b>\$ 54,787</b>

\* During the first quarter of 2015, we changed the methodology for allocating certain unallocated expenses to our segments. The prior period information has been adjusted to consistently reflect this change.

We are exposed to a concentration of revenue from the U.S. Military Air Mobility Command (the AMC) and Polar (see Note 3 for further discussion regarding Polar). No other customer accounted for more than 10.0% of our Total Operating Revenue. Revenue from the AMC was \$114.0 million for the three months ended June 30, 2015 and \$91.3 million for the three months ended June 30, 2014. Revenue from the AMC was \$204.1 million for the six months ended June 30, 2015 and \$154.2 million for the six months ended June 30, 2014. Accounts receivable from the AMC were \$19.5 million and \$15.3 million as of June 30, 2015 and December 31, 2014, respectively. We have not

experienced any credit issues with either of these customers.

## **10. Legal Proceedings**

### ***Matters Related to Alleged Pricing Practices***

The Company and Old Polar have been named defendants, along with a number of other cargo carriers, in several class actions in the United States arising from allegations about the pricing practices of Old Polar and a number of air cargo carriers that have now been centralized for pretrial purposes in the United States District Court for the Eastern District of New York. The consolidated complaint alleges, among other things, that the defendants, including the Company and Old Polar, manipulated the market price for air cargo services sold domestically and abroad through the use of surcharges, in violation of United States, state, and European Union antitrust laws. The suit seeks treble damages and injunctive relief.

In 2007, the Company and Old Polar commenced an adversary proceeding in bankruptcy court against each of the plaintiffs in this class action litigation seeking to enjoin the plaintiffs from prosecuting claims against the Company and Old Polar that arose prior to July 28, 2004, the date on which the Company and Old Polar emerged from bankruptcy. In 2007, the plaintiffs consented to the injunctive relief requested and the bankruptcy court entered an order enjoining plaintiffs from prosecuting Company claims arising prior to July 28, 2004.

The court in the antitrust class actions has heard and decided a number of procedural motions. Among those was the plaintiffs' motion to join Polar Air Cargo Worldwide, Inc. as an additional defendant, which the court granted for discovery

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purposes on April 13, 2011. There was substantial pretrial written discovery and document production, and a number of depositions were taken. A court hearing on whether to certify the case as a class action was held in October 2013, and oral arguments and an evidentiary hearing were held in November 2013. On October 15, 2014, the magistrate judge issued a decision recommending that the court enter an order certifying the class for adjudicating the claims. On July 10, 2015, the court issued an order affirming the magistrate judge's decision and certifying the class. We and other remaining defendants have petitioned the U.S. Court of Appeals for the Second Circuit for permission to appeal that order and we also intend to vigorously pursue a number of defenses, some of which were made in summary judgment motions and responses in 2015. We are unable to reasonably predict the court's ruling on our opposition to class certification and our defenses, or the ultimate outcome of the litigation.

In the United Kingdom, several groups of named claimants have brought suit against British Airways in connection with the same alleged antitrust practices at issue in the proceedings described above and are seeking damages allegedly arising from that conduct. British Airways has filed claims in the lawsuit against Old Polar, the Company and a number of air cargo carriers for contribution should British Airways be found liable to claimants. Old Polar's formal statement of defense was filed on February 28, 2015. Court-ordered disclosure is continuing. Old Polar intends to mount a vigorous defense.

If the Company or Old Polar were to incur an unfavorable outcome in connection with one or more of the matters described above, such outcome is not expected to materially affect our business, financial condition, results of operations or cash flows.

### ***Brazilian Customs Claim***

Old Polar was cited for two alleged customs violations in Sao Paulo, Brazil, relating to shipments of goods dating back to 1999 and 2000. Each claim asserts that goods listed on the flight manifest of two separate Old Polar scheduled service flights were not on board the aircraft upon arrival and therefore were improperly brought into Brazil. The two claims, which also seek unpaid customs duties, taxes and penalties from the date of the alleged infraction, are approximately \$6.3 million in aggregate based on June 30, 2015 exchange rates.

In both cases, we believe that the amounts claimed are substantially overstated due to a calculation error when considering the type and amount of goods allegedly missing, among other things. Furthermore, we may seek appropriate indemnity from the shipper in each claim as may be feasible. In the pending claim for one of the cases, we have received an administrative decision dismissing the claim in its entirety, which remains subject to a mandatory appeal by the Brazil customs authorities. As required to defend such claims, we have made deposits pending resolution of these matters. The balances were \$4.7 million as of June 30, 2015 and \$5.3 million as of December 31, 2014, and are included in Deposits and other assets.

We are currently defending these and other Brazilian customs claims and the ultimate disposition of these claims, either individually or in the aggregate, is not expected to materially affect our financial condition, results of operations or cash flows.

### ***Other***

We have certain other contingencies incident to the ordinary course of business. Management believes that the ultimate disposition of such other contingencies is not expected to materially affect our financial condition, results of operations or cash flows.

## **11. Earnings Per Share**

Basic earnings per share ( EPS ) represent net income attributable to common shareholders divided by the weighted average number of common shares outstanding during the measurement period. Diluted EPS represent net income attributable to common shareholders divided by the weighted average number of common shares outstanding during the measurement period while also giving effect to all potentially dilutive common shares that were outstanding during the period using the treasury stock method. Anti-dilutive shares related to warrants and stock options that were out of the money and excluded for the three and six months ended June 30, 2015 were 3.0 million and for the three and six months ended June 30, 2014 were de minimis.

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The calculations of basic and diluted EPS were as follows:

	<b>For the Three Months Ended</b>		<b>For the Six Months Ended</b>	
	<b>June 30, 2015</b>	<b>June 30, 2014</b>	<b>June 30, 2015</b>	<b>June 30, 2014</b>
<b>Numerator:</b>				
Net Income Attributable to Common Stockholders	\$ 28,390	\$ 29,593	\$ 57,622	\$ 37,537
<b>Denominator:</b>				
Basic EPS weighted average shares outstanding	25,029	25,241	24,953	25,169
Effect of dilutive stock options and restricted stock	169	38	182	46
Diluted EPS weighted average shares outstanding	25,198	25,279	25,135	25,215
<b>EPS:</b>				
Basic	\$ 1.13	\$ 1.17	\$ 2.31	\$ 1.49
Diluted	\$ 1.13	\$ 1.17	\$ 2.29	\$ 1.49

The calculation of EPS does not include restricted share units in which performance or market conditions were not satisfied of 0.3 million for the three and six months ended June 30, 2015, respectively, and 0.4 million and 0.5 million for the three and six months ended June 30, 2014, respectively.

**12. Accumulated Other Comprehensive Income (Loss)**

The following table summarizes the components of Accumulated other comprehensive income (loss):

	<b>Interest Rate Derivatives</b>	<b>Foreign Currency Translation</b>	<b>Total</b>
Balance as of December 31, 2013	\$ (11,375)	\$ 698	\$ (10,677)
Net change in fair value	(251)		(251)
Reclassification to interest expense	1,372		1,372
Translation adjustment		171	171
Tax effect	(506)		(506)
Balance as of June 30, 2014	\$ (10,760)	\$ 869	\$ (9,891)

	<b>Interest Rate Derivatives</b>	<b>Foreign Currency Translation</b>	<b>Total</b>
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Balance as of December 31, 2014	\$ (9,924)	\$ 352	\$ (9,572)
Net change in fair value			
Reclassification to interest expense	1,288		1,288
Translation adjustment		(343)	(343)
Tax effect	(492)		(492)
Balance as of June 30, 2015	\$ (9,128)	\$ 9	\$ (9,119)

***Interest Rate Derivatives***

As of June 30, 2015, there was \$14.7 million of unamortized realized loss before taxes remaining in Accumulated other comprehensive income (loss) related to terminated forward-starting interest rate swaps, which had been designated as cash flow hedges to effectively fix the interest rates on two 747-8F financings in 2011 and three 777-200LRF financings in 2014. The net loss is amortized and reclassified into Interest expense over the remaining life of the related debt. Net realized losses reclassified into earnings were \$0.6 million and \$0.7 for the three months ended June 30, 2015 and 2014, respectively. Net realized losses reclassified into earnings were \$1.3 million and \$1.4 million for the six months ended June 30, 2015 and 2014, respectively. Net realized losses expected to be reclassified into earnings within the next 12 months are \$2.5 million as of June 30, 2015.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis should be read in conjunction with our unaudited Financial Statements appearing in this report and our audited consolidated financial statements and related notes included in our 2014 Annual Report on Form 10-K.

**Background**

**Certain Terms - Glossary**

The following represents terms and statistics specific to our business and industry. They are used by management to evaluate and measure operations, results, productivity and efficiency.

Block Hour	The time interval between when an aircraft departs the terminal until it arrives at the destination terminal.
C Check	High-level or heavy airframe maintenance checks, which are more intensive in scope than Line Maintenance and are generally performed between 18 and 24 months depending on aircraft type.
D Check	High-level or heavy airframe maintenance checks, which are the most extensive in scope and are generally performed every six and eight years depending on aircraft type.
Heavy Maintenance	Scheduled maintenance activities, which are the most extensive in scope and are primarily based on time intervals, including, but not limited to, C Checks, D Checks and engine overhauls. In addition, unscheduled engine repairs involving the removal of the engine from the aircraft are considered to be heavy maintenance. Heavy maintenance can generally take from one to eight weeks to complete.
Line Maintenance	Unscheduled maintenance to rectify events occurring during normal day-to-day operations.
Non-heavy	Discrete maintenance activities for the overhaul and repair of specific aircraft
Maintenance	components, including landing gear, auxiliary power units and engine thrust reversers.
Yield	The average amount a customer pays to fly one tonne of cargo one mile.

**Business Overview**

We are a leading global provider of outsourced aircraft and aviation operating services, operating the world's largest fleet of 747 freighters, as well as operating 747 and 767 passenger aircraft and 767 freighters. We also own and dry lease a portfolio of aircraft, including six 777 freighters. We provide unique value to our customers by giving them access to highly reliable new production freighters that deliver the lowest unit cost in the marketplace combined with outsourced aircraft operating services that we believe lead the industry in terms of quality and global scale. Our customers include airlines, express delivery providers, freight forwarders, the U.S. military and charter brokers. We provide global services with operations in Africa, Asia, Australia, Europe, the Middle East, North America and South America.



Our primary service offerings include the following:

ACMI, whereby we provide outsourced cargo and passenger aircraft operating solutions, including the provision of an aircraft, crew, maintenance and insurance, while customers assume fuel, demand and Yield risk. In addition, the customer is responsible for landing, navigation and most other operational fees and costs;

CMI, which is part of our ACMI business segment, whereby we provide outsourced cargo and passenger aircraft operating solutions, including the provision of crew, maintenance and insurance, while customers provide the aircraft and assume fuel, demand and Yield risk. In addition, the customer is responsible for landing, navigation and most other operational fees and costs;

Charter, whereby we provide cargo and passenger aircraft charter services to customers, including the AMC, brokers, freight forwarders, direct shippers, airlines, sports teams and fans, and private charter customers. The customer pays a fixed charter fee that includes fuel, insurance, landing fees, navigation fees and most other operational fees and costs; and

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Dry Leasing, whereby we provide cargo and passenger aircraft and engine leasing solutions. The customer operates, and is responsible for insuring and maintaining, the flight equipment. We look to achieve our growth plans and enhance shareholder value by:

Delivering superior service quality to our valued customers;

Aggressively managing our fleet with a focus on leading-edge aircraft;

Focusing on securing long-term customer contracts;

Driving significant and ongoing productivity improvements;

Selectively pursuing and evaluating future acquisitions and alliances; while

Appropriately managing capital allocation and returning capital to shareholders.

See **Business Overview** and **Business Strategy** in our 2014 Annual Report on Form 10-K for additional information.

**Business Developments**

Our ACMI results for 2015, compared with 2014, were impacted by the following events:

In February 2014, we began ACMI flying a 747-8F aircraft with BST Logistics (Hong Kong) Company Limited, a business partner of Navitrans International Freight Forwarding Co., Ltd. Service, which was the first 747-8F aircraft in its network.

In April and early May 2014, British Airways returned three 747-8F aircraft. In May and October 2014, the three 747-8F aircraft were placed in ACMI service for DHL, replacing one 747-400F aircraft.

In October 2014, we began ACMI flying one additional 747-400F aircraft for DHL, increasing the number of 747 freighter aircraft in ACMI service for DHL to twelve.

In November 2014, we began ACMI flying a 747-400F aircraft for Etihad Airways, which was the second 747-400F aircraft in its global network.

In March 2015, we began ACMI flying one additional 747-8F aircraft for DHL following its transition from Panalpina Air & Ocean Ltd. The aircraft is initially replacing a 747-400F aircraft.

In the first quarter of 2015, we began CMI flying three additional 767-200 freighters owned by DHL in its North American network. A fourth 767-200 freighter began CMI flying in April 2015.

In June 2015, we signed an ACMI agreement with DHL for one additional 747-400F aircraft, increasing the number of 747 freighter aircraft in ACMI service for DHL to thirteen. The aircraft began flying in July 2015.

Charter Block Hours increased during the first half of 2015, reflecting increased cargo and passenger demand from the AMC and stronger commercial cargo demand, which was enhanced by the U.S. West Coast port disruption. In June 2015, based on this demand, we returned to active service a 747-400BCF that had been temporarily parked. We also entered into a short-term operating lease beginning in late June for a second 747-400 converted freighter. This lease, with terms that are more favorable to us, is intended to replace a similar aircraft, with a lease that expired in June 2015.

During the second quarter of 2015, we Dry Leased a 757-200 freighter to DHL on a long-term basis, following the conclusion of a previous customer lease. We also acquired and are converting two 767-300 passenger aircraft to freighters. Following their conversion, which is expected to be completed during the fourth quarter of 2015, they will be Dry Leased to DHL on a long-term basis.

**Table of Contents****Results of Operations**

The following discussion should be read in conjunction with our Financial Statements and other financial information appearing and referred to elsewhere in this report.

**Three Months Ended June 30, 2015 and 2014****Operating Statistics**

The table below sets forth selected Operating Statistics for the three months ended June 30:

	2015	2014	Increase / (Decrease)	Percent Change
<b>Block Hours</b>				
ACMI	30,958	27,652	3,306	12.0%
Charter:				
Cargo	9,214	7,572	1,642	21.7%
Passenger	4,259	3,487	772	22.1%
Other	303	299	4	1.3%
<b>Total Block Hours</b>	<b>44,734</b>	<b>39,010</b>	<b>5,724</b>	<b>14.7%</b>
<b>Revenue Per Block Hour</b>				
ACMI	\$ 6,113	\$ 6,752	\$ (639)	(9.5)%
Charter:	\$ 17,475	\$ 20,367	\$ (2,892)	(14.2)%
Cargo	\$ 16,358	\$ 20,035	\$ (3,677)	(18.4)%
Passenger	\$ 19,891	\$ 21,087	\$ (1,196)	(5.7)%
<b>Charter Fuel</b>				
Average fuel cost per gallon	\$ 2.46	\$ 3.19	\$ (0.73)	(22.9)%
Fuel gallons consumed (000s)	39,383	32,560	6,823	21.0%
<b>Segment Operating Fleet (average aircraft equivalents during the period)</b>				
<b>ACMI*</b>				
747-8F Cargo	9.0	8.3	0.7	
747-400 Cargo	11.4	11.7	(0.3)	
747-400 Dreamlifter	3.1	3.3	(0.2)	
767-300 Cargo	2.0	2.0		
767-200 Cargo	8.9	5.0	3.9	
747-400 Passenger	1.0	1.0		
767-200 Passenger	1.0	1.0		
<b>Total</b>	<b>36.4</b>	<b>32.3</b>	<b>4.1</b>	

**Charter**

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747-8F Cargo		0.7	(0.7)
747-400 Cargo	10.5	9.1	1.4
747-400 Passenger	2.0	1.9	0.1
767-300 Passenger	2.9	3.0	(0.1)
<b>Total</b>	<b>15.4</b>	<b>14.7</b>	<b>0.7</b>
<b>Dry Leasing</b>			
777-200 Cargo	6.0	6.0	
757-200 Cargo	1.0	1.0	
737-300 Cargo	1.0	1.0	
737-800 Passenger	1.0	2.0	(1.0)
<b>Total</b>	<b>9.0</b>	<b>10.0</b>	<b>(1.0)</b>
<b>Total Operating Aircraft</b>	<b>60.8</b>	<b>57.0</b>	<b>3.8</b>
<b>Out-of-service**</b>	<b>0.8</b>	<b>1.0</b>	<b>(0.2)</b>

\* ACMI average fleet excludes spare aircraft provided by CMI customers.

\*\* Our out-of-service aircraft are completely unencumbered.

**Table of Contents****Operating Revenue**

The following table compares our Operating Revenue for the three months ended June 30 (in thousands):

	2015	2014	Increase / (Decrease)	Percent Change
<b>Operating Revenue</b>				
ACMI	\$ 189,255	\$ 186,720	\$ 2,535	1.4%
Charter	235,436	225,234	10,202	4.5%
Dry Leasing	27,401	25,524	1,877	7.4%
Other	3,741	3,691	50	1.4%
<b>Total Operating Revenue</b>	<b>\$ 455,833</b>	<b>\$ 441,169</b>	<b>\$ 14,664</b>	<b>3.3%</b>

*ACMI revenue* increased \$2.5 million, or 1.4%, primarily due to increased flying, partially offset by reduced Revenue per Block Hour. ACMI Block Hours were 30,958 in the second quarter of 2015, compared with 27,652 in 2014, an increase of 3,306 Block Hours, or 12.0%. The increase in Block Hours was primarily driven by the start-up of CMI flying four additional 767-200F aircraft and improvements in ACMI aircraft utilization. ACMI Revenue per Block Hour was \$6,113 for the second quarter of 2015, compared with \$6,752 in 2014, a decrease of \$639 per Block Hour, or 9.5%. The decrease in Revenue per Block Hour reflects the impact of payments received in 2014 related to a customer's return of aircraft and increased CMI flying in 2015.

*Charter revenue* increased \$10.2 million, or 4.5%, primarily driven by an increase in both cargo and passenger flying, partially offset by a decrease in Revenue per Block Hour. Charter Block Hours were 13,473 in the second quarter of 2015 compared with 11,059 in 2014, an increase of 2,414 Block Hours, or 21.8%. The increase in Charter Block Hours was primarily driven by increased passenger and cargo demand from the AMC and increased commercial cargo demand. Charter Revenue per Block Hour was \$17,475 for the second quarter of 2015 compared with \$20,367 in 2014, a decrease of \$2,892 per Block Hour, or 14.2%. This decrease was primarily driven by the impact of lower fuel prices.

*Dry Leasing revenue* increased \$1.9 million, or 7.4%, primarily due to revenue from maintenance payments related to the scheduled return of a 757-200 cargo aircraft in April 2015.

**Operating Expenses**

The following table compares our Operating Expenses for the three months ended June 30 (in thousands):

	2015	2014	Increase / (Decrease)	Percent Change
<b>Operating Expenses</b>				
Salaries, wages and benefits	\$ 86,862	\$ 77,948	\$ 8,914	11.4%
Aircraft fuel	96,711	103,842	(7,131)	(6.9)%
Maintenance, materials and repairs	41,438	50,386	(8,948)	(17.8)%
Aircraft rent	36,811	34,826	1,985	5.7%

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Depreciation and amortization	31,936	30,381	1,555	5.1%
Navigation fees, landing fees and other rent	22,666	30,906	(8,240)	(26.7)%
Travel	23,830	18,774	5,056	26.9%
Passenger and ground handling services	21,353	21,859	(506)	(2.3)%
Loss on disposal of aircraft	114	14,679	(14,565)	NM
Special charge	499	1,449	(950)	NM
Other	32,329	29,462	2,867	9.7%
<b>Total Operating Expenses</b>	<b>\$ 394,549</b>	<b>\$ 414,512</b>		

NM represents year-over-year changes that are not meaningful.

*Salaries, wages and benefits* increased \$8.9 million, or 11.4%, primarily driven by increases to crewmember and ground staff costs due to higher Block Hours, key initiatives and increased profitability.

*Aircraft fuel* decreased \$7.1 million, or 6.9%, primarily due to fuel price decreases, partially offset by increased fuel consumption. The average fuel price per gallon for the Charter business was \$2.46 for the second quarter of 2015, compared with \$3.19 in 2014, a decrease of 22.9%. Fuel consumption increased by 6.8 million gallons, or 21.0%, reflecting the increase in Charter Block Hours operated. We do not incur fuel expense in our ACMI or Dry Leasing businesses as the cost of fuel is borne by the customer.

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*Maintenance, materials and repairs* decreased \$8.9 million, or 17.8%, primarily reflecting a decrease of \$9.4 million for 747-400 aircraft. Heavy Maintenance on 747-400 aircraft decreased \$7.2 million due to a decrease in the number of C and D Checks, and the number of engine overhauls. Non-heavy Maintenance on 747-400 aircraft decreased \$1.5 million. Heavy Maintenance expense on 747-8F aircraft was relatively unchanged. Heavy airframe maintenance events and engine overhauls for the three months ended June 30 were:

<b>Heavy Maintenance Events</b>	<b>2015</b>	<b>2014</b>	<b>Increase / (Decrease)</b>
747-8F C Checks		2	(2)
747-400 C Checks	2	3	(1)
767 C Checks		1	(1)
747-400 D Checks	1	2	(1)
CF6-80 engine overhauls	1	2	(1)

*Aircraft rent* increased \$2.0 million, or 5.7%, primarily due to the return to service of a leased 747-400BCF aircraft that had been previously parked.

*Depreciation and amortization* increased \$1.6 million, or 5.1%, primarily due to increased scrapping of rotatable parts related to our engine and spare parts purchase program, which avoids more expensive repairs.

*Navigation fees, landing fees and other rent* decreased \$8.2 million, or 26.7%, primarily due to a reduction in purchased capacity from the subcontracting of certain Charter flights.

*Travel* increased \$5.1 million, or 26.9%, primarily due to higher rates related to crewmember travel to higher cost locations and increased flying.

*Loss on disposal of aircraft* in 2014 resulted from the trade-in of used spare engines for new engines as part of our engine acquisition program.

*Other* increased \$2.9 million, or 9.7%, primarily due to increased commission expense on higher revenue from the AMC and increased professional fees to support key initiatives.

**Non-operating Expenses (Income)**

The following table compares our Non-operating Expenses (Income) for the three months ended June 30 (in thousands):

	<b>2015</b>	<b>2014</b>	<b>Increase / (Decrease)</b>	<b>Percent Change</b>
<b>Non-operating Expenses (Income)</b>				
Interest income	\$ (4,425)	\$ (4,719)	\$ (294)	(6.2)%
Interest expense	25,033	26,365	(1,332)	(5.1)%
Capitalized interest	(177)	(67)	110	164.2%
Other expense (income), net	(284)	(88)	196	NM



*Interest expense* decreased \$1.3 million, or 5.1%, primarily due to a decrease in our average debt balances, reflecting payments of debt, partially offset by the issuance of the Convertible Notes.

*Income taxes.* Our effective income tax rates were an expense of 31.0% for the three months ended June 30, 2015 and a benefit of 461.0% for the three months ended June 30, 2014. The effective income tax rate for the three months ended June 30, 2015 differed from the U.S. federal statutory rate primarily due to our assertion, beginning in 2013, to indefinitely reinvest the net earnings of certain foreign subsidiaries outside the U.S. The effective income tax rate for the three months ended June 30, 2014 differed from the U.S. federal statutory rate primarily due to an income tax benefit of \$24.0 million, net of reserves, related to ETI (see Note 7 to our Financial Statements) and our assertion, beginning in 2013, to indefinitely reinvest the net earnings of certain foreign subsidiaries outside the U.S.

**Table of Contents****Segments**

The following table compares the Direct Contribution of our reportable segments (see Note 9 to our Financial Statements for the reconciliation to Operating income) for the three months ended June 30 (in thousands):

	2015	2014	Increase / (Decrease)	Percent Change
<b>Direct Contribution:</b>				
ACMI	\$ 51,157	\$ 44,677	\$ 6,480	14.5%
Charter	25,019	8,196	16,823	205.3%
Dry Leasing	10,894	8,738	2,156	24.7%
<b>Total Direct Contribution</b>	<b>\$ 87,070</b>	<b>\$ 61,611</b>	<b>\$ 25,459</b>	<b>41.3%</b>
Unallocated income and expenses, net	\$ 45,320	\$ 40,317	\$ 5,003	12.4%

***ACMI Segment***

ACMI Direct Contribution increased \$6.5 million, or 14.5%, primarily due to higher aircraft utilization and a reduction in Heavy maintenance expense, partially offset by lower Revenue per Block Hour.

***Charter Segment***

Charter Direct Contribution increased \$16.8 million, or 205.3%, primarily due to increased cargo and passenger flying, as well as higher aircraft utilization. In addition, Charter Direct Contribution benefited from a reduction in Heavy maintenance expense.

***Dry Leasing Segment***

Dry Leasing Direct Contribution increased \$2.2 million, or 24.7%, primarily due to revenue from maintenance payments related to the scheduled return of a 757-200 cargo aircraft in April 2015.

***Unallocated income and expenses, net***

Unallocated income and expenses, net increased \$5.0 million, or 12.4%, primarily due to the timing of incentive compensation driven by higher anticipated earnings in 2015, increased professional fees to support key initiatives and unallocated interest expense.

**Table of Contents****Six Months Ended June 30, 2015 and 2014****Operating Statistics**

The following discussion should be read in conjunction with our Financial Statements and notes thereto and other financial information appearing and referred to elsewhere in this report.

The table below sets forth selected Operating Statistics for the six months ended June 30:

	2015	2014	Increase / (Decrease)	Percent Change
<b>Block Hours</b>				
ACMI	60,418	55,675	4,743	8.5%
<b>Charter:</b>				
Cargo	17,482	13,471	4,011	29.8%
Passenger	7,480	6,202	1,278	20.6%
Other	634	535	99	18.5%
<b>Total Block Hours</b>	<b>86,014</b>	<b>75,883</b>	<b>10,131</b>	<b>13.4%</b>
<b>Revenue Per Block Hour</b>				
ACMI	\$ 6,261	\$ 6,913	\$ (652)	(9.4)%
Charter:	\$ 18,251	\$ 20,465	\$ (2,214)	(10.8)%
Cargo	\$ 17,724	\$ 20,148	\$ (2,424)	(12.0)%
Passenger	\$ 19,482	\$ 21,154	\$ (1,672)	(7.9)%
<b>Charter Fuel</b>				
Average fuel cost per gallon	\$ 2.40	\$ 3.21	\$ (0.81)	(25.2)%
Fuel gallons consumed (000s)	72,694	57,859	14,835	25.6%
<b>Segment Operating Fleet (average aircraft equivalents during the period)</b>				
<b>ACMI*</b>				
747-8F Cargo	8.8	8.5	0.3	
747-400 Cargo	11.7	12.1	(0.4)	
747-400 Dreamlifter	3.1	3.2	(0.1)	
767-300 Cargo	2.0	2.0		
767-200 Cargo	7.7	5.0	2.7	
747-400 Passenger	1.0	1.0		
767-200 Passenger	1.0	1.0		
<b>Total</b>	<b>35.3</b>	<b>32.8</b>	<b>2.5</b>	
<b>Charter</b>				
747-8F Cargo	0.2	0.4	(0.2)	
747-400 Cargo	9.7	8.8	0.9	
747-400 Passenger	2.0	2.0		

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767-300 Passenger	2.9	2.9	
<b>Total</b>	<b>14.8</b>	<b>14.1</b>	<b>0.7</b>
<b>Dry Leasing</b>			
777-200 Cargo	6.0	5.9	0.1
757-200 Cargo	1.0	1.0	
737-300 Cargo	1.0	1.0	
737-800 Passenger	1.3	2.0	(0.7)
<b>Total</b>	<b>9.3</b>	<b>9.9</b>	<b>(0.6)</b>
<b>Total Operating Aircraft</b>	<b>59.4</b>	<b>56.8</b>	<b>2.6</b>
<b>Out-of-service**</b>	<b>0.9</b>	<b>1.0</b>	<b>(0.1)</b>

\* ACMI average fleet excludes spare aircraft provided by CMI customers.

\*\* All of our out-of-service aircraft are completely unencumbered.

**Table of Contents****Operating Revenue**

The following table compares our Operating Revenue for the six months ended June 30 (in thousands):

	2015	2014	Increase / (Decrease)	Percent Change
<b>Operating Revenue</b>				
ACMI	\$ 378,302	\$ 384,861	\$ (6,559)	(1.7)%
Charter	455,574	402,607	52,967	13.2%
Dry Leasing	59,320	50,200	9,120	18.2%
Other	7,482	6,864	618	9.0%
<b>Total Operating Revenue</b>	<b>\$ 900,678</b>	<b>\$ 844,532</b>	<b>\$ 56,146</b>	<b>6.6%</b>

*ACMI revenue* decreased \$6.6 million, or 1.7%, primarily due to reduced Revenue per Block Hour, partially offset by increased flying. ACMI Revenue per Block Hour was \$6,261 for the first half of 2015, compared with \$6,913 in 2014, a decrease of \$652 per Block Hour, or 9.4%. The decrease in Revenue per Block Hour reflects the impact of higher Revenue per Block Hour in 2014 resulting from customers that flew below their contractual minimums, payments received in 2014 related to a customer's return of aircraft, and increased CMI flying in 2015. ACMI Block Hours were 60,418 for the first half of 2015, compared with 55,675 in 2014, an increase of 4,743 Block Hours, or 8.5%. The increase in Block Hours was primarily driven by the start-up of CMI flying four additional 767-200F aircraft and improvements in ACMI aircraft utilization.

*Charter revenue* increased \$53.0 million, or 13.2%, primarily driven by an increase in both cargo and passenger flying, partially offset by a decrease in Revenue per Block Hour. Charter Block Hours were 24,962 for the first half of 2015 compared with 19,673 in 2014, an increase of 5,289 Block Hours, or 26.9%. The increase in Charter Block Hours was primarily driven by increased cargo and passenger demand from the AMC and increased commercial cargo demand, which was enhanced by the U.S. West Coast port disruption. Charter Revenue per Block Hour was \$18,251 for the first half of 2015 compared with \$20,465 in 2014, a decrease of \$2,214 per Block Hour, or 10.8%. This decrease was primarily driven by the impact of lower fuel prices.

*Dry Leasing revenue* increased \$9.1 million, or 18.2%, primarily due to revenue from maintenance payments related to the scheduled returns of a 737-800 passenger aircraft in February 2015 and a 757-200 cargo aircraft in April 2015.

**Operating Expenses**

The following table compares our Operating Expenses for the six months ended June 30 (in thousands):

	2015	2014	Increase / (Decrease)	Percent Change
<b>Operating Expenses</b>				
Salaries, wages and benefits	\$ 175,635	\$ 150,803	\$ 24,832	16.5%
Aircraft fuel	174,826	185,586	(10,760)	(5.8)%
Maintenance, materials and repairs	100,270	109,432	(9,162)	(8.4)%

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Aircraft rent	71,072	70,236	836	1.2%
Depreciation and amortization	63,966	58,536	5,430	9.3%
Navigation fees, landing fees and other rent				