MESA AIR GROUP INC
Form 10-K
December 14, 2006

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

Form 10-K

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

For the Fiscal Year Ended September 30, 2006

Commission File Number 0-15495

Mesa Air Group, Inc.
(Exact name of registrant as specified in its charter)

Nevada	**85-0302351**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
410 North 44th Street, Suite 100, Phoenix, Arizona	**85008**
(Address of principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code:
(602) 685-4000

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock. No Par Value	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes o No þ

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 þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant as of December 1, 2006: Common Stock, no par value: $270.3 million.

On December 1, 2006, the Registrant had outstanding 33,956,878 shares of Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

Certain sections of the Company s Proxy Statement to be filed in connection with the Company s 2007 Annual Meeting of Stockholders to be held in March 2007 are incorporated by herein at Part III, Items 10-14.

MESA AIR GROUP, INC.

2006 FORM 10-K REPORT

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PART I

Forward-Looking Statements

This Form 10-K Report contains certain statements including, but not limited to, information regarding the replacement, deployment, and acquisition of certain numbers and types of aircraft, and projected expenses associated therewith; costs of compliance with Federal Aviation Administration regulations and other rules and acts of Congress; the passing of taxes, fuel costs, inflation, and various expenses to the consumer; the relocation of certain operations of Mesa; the resolution of litigation in a favorable manner and certain projected financial obligations. These statements, in addition to statements made in conjunction with the words expect, anticipate, intend, plan, believe, seek, estimate, and similar expressions, are forward-looking statements within the meaning of the Safe Harbor provision of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements relate to future events or the future financial performance of Mesa and only reflect management s expectations and estimates. The following is a list of factors, among others, that could cause actual results to differ materially from the forward-looking statements: changing business conditions in certain market segments and industries; changes in Mesa s code-sharing relationships; the inability of Delta Air Lines, US Airways or United Airlines to pay their obligations under the code-share agreements; the inability of Delta Air Lines to successfully restructure and emerge from bankruptcy; the ability of Delta Air Lines to reject our regional jet code-share agreement in bankruptcy; an increase in competition along the routes Mesa operates or plans to operate; material delays in completion by the manufacturer of the ordered and yet-to-be delivered aircraft; availability and cost of funds for financing new aircraft; changes in general economic conditions; changes in fuel price; changes in regional economic conditions; Mesa s relationship with employees and the terms of future collective bargaining agreements; the impact of current and future laws; additional terrorist attacks; Congressional investigations, and governmental regulations affecting the airline industry and Mesa s operations; bureaucratic delays; amendments to existing legislation; consumers unwilling to incur greater costs for flights; our ability to operate our new Hawaiian airline service profitably; unfavorable resolution of legal proceedings involving Hawaiian Airlines and Aloha Airlines regarding our Hawaiian operation; unfavorable resolution of negotiations with municipalities for the leasing of facilities; and risks associated with the outcome of litigation. One or more of these or other factors may cause Mesa s actual results to differ materially from any forward-looking statement. Mesa is not undertaking any obligation to update any forward-looking statements contained in this Form 10-K.

All references to we, our, us, or Mesa refer to Mesa Air Group, Inc. and its predecessors, direct and indirect subsidiaries and affiliates.

Item 1. *Business*

General

Mesa Air Group, Inc. (Mesa or the Company) is a holding company whose principal subsidiaries operate as regional air carriers providing scheduled passenger and airfreight service. As of September 30, 2006, the Company served 173 cities in 46 states, the District of Columbia, Canada, the Bahamas and Mexico and operated a fleet of 191 aircraft with approximately 1,200 daily departures.

Approximately 98% of our consolidated passenger revenues for the fiscal year ended September 30, 2006 were derived from operations associated with code-share agreements. Our subsidiaries have code-share agreements with Delta Air Lines, Inc. (Delta), Midwest Airlines, Inc. (Midwest Airlines), United Airlines, Inc. (United Airlines or

United) and America West Airlines, Inc. (America West) which currently operates as US Airways and is referred to herein as US Airways. The current US Airways is a result of a merger between America West and US Airways, Inc. (Pre-Merger US Airways). These code-share agreements allow use of the code-share partners flight designator code to identify flights and fares in computer reservation systems, permit use of logos, service marks, aircraft paint schemes and uniforms similar to the code-share partner and provide coordinated schedules and joint advertising. The remaining passenger revenues are derived from our independent operations Mesa Airlines and ***go!***

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In addition to carrying passengers, we carry freight and express packages on our passenger flights and have interline small cargo freight agreements with many other carriers. We also have contracts with the U.S. Postal Service for carriage of mail to the cities we serve and occasionally operate charter flights when our aircraft are not otherwise used for scheduled service.

Our airline operations are conducted by the following airline subsidiaries:

Mesa Airlines, Inc. (Mesa Airlines), a Nevada corporation, flies regional jet and turboprop aircraft and operates as US Airways Express under code-share agreements with US Airways, as United Express under a code-share agreement with United Airlines and independently in Hawaii as ***go!*** The ***go!*** flights are Independent Operations and are not subject to a code-sharing agreement with a major carrier.

Air Midwest, Inc. (Air Midwest), a Kansas corporation, flies Beechcraft 1900D 19-seat turboprop aircraft and operates as US Airways Express under code-share agreements with US Airways and Pre-Merger US Airways. Air Midwest s flights in Kansas City code-share with both Midwest Airlines and US Airways. Air Midwest also operates as Mesa Airlines in select Essential Air Service (EAS) markets. The Albuquerque flights and certain EAS markets are Independent Operations and are not subject to a code-sharing agreement with a major carrier.

Freedom Airlines, Inc. (Freedom), a Nevada corporation, flies ERJ-145 50-seat regional jets and 37-seat Dash-8 turboprop aircraft and operates as Delta Connection under code-share agreements with Delta.

Unless the context indicates otherwise, the terms Mesa, the Company, we, us, or our, refer to Mesa Air Group, I and its subsidiaries.

Corporate Structure

Mesa is a Nevada corporation with its principal executive office in Phoenix, Arizona.

In addition to operating the airline subsidiaries listed above, we also have the following other subsidiaries:

MPD, Inc., a Nevada corporation, doing business as Mesa Pilot Development and MPD, operates training programs for student pilots in conjunction with San Juan College in Farmington, New Mexico and Arizona State University in Tempe, Arizona.

Regional Aircraft Services, Inc., (RAS) a California corporation, performs aircraft component repair, certain overhaul services, and ground handling services, primarily to Mesa subsidiaries.

MAGI Insurance, Ltd., a Barbados, West Indies based captive insurance company, was established for the purpose of obtaining more favorable aircraft liability insurance rates.

Ritz Hotel Management Corp., a Nevada Corporation, was established to facilitate the Company s acquisition and management of a Phoenix area hotel property used for crew-in-training accommodations.

Mesa Air Group Airline Inventory Management, LLC (MAG-AIM), an Arizona Limited Liability Company, was established to purchase, distribute and manage Mesa s inventory of spare rotable and expendable parts.

Nilchii, Inc., a Nevada corporation, was established to invest in certain airline related businesses.

Air Midwest, LLC, a Nevada limited liability company, was formed for the purpose of a contemplated conversion of Air Midwest, Inc. from a corporation to a limited liability company. This conversion has not yet occurred.

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Aircraft in Operation

The following table sets forth our aircraft fleet (owned and leased) in operation by aircraft type and code-share service as of September 30, 2006:

	Canadair Regional Jet-200 (CRJ-200)	Canadair Regional Jet-700 (CRJ-700)	Canadair Regional Jet-900 (CRJ-900)	Embraer Regional Jet-145 (ERJ-145)	Beechcraft 1900D	DeHavilland Dash 8	Total
US Airways Express	18		38		16	6	78
United Express	37	15		8		10	70
Delta Connection				28		6	34
Mesa Airlines	5				4		9
Total	60	15	38	36	20	22	191

Code-Share Agreements

Our airline subsidiaries have agreements with Delta, US Airways, United Airlines and Midwest Airlines to use those carriers designation codes (commonly referred to as code-share agreements). These code-share agreements allow use of the code-share partner s flight designator code to identify flights and fares in computer reservation systems, permit use of logos, service marks, aircraft paint schemes and uniforms similar to the code-share partner s and provide coordinated schedules and joint advertising. Our passengers traveling on flights operated pursuant to code-share agreements receive mileage credits in the respective frequent flyer programs of our code-share partners, and credits in those programs can be used on flights operated by us.

The financial arrangement with our code-share partners involves either a revenue-guarantee or pro-rate arrangement. The US Airways (regional jet and Dash-8), Delta (regional jet and Dash-8) and United (regional jet and Dash-8) code-share agreements are revenue-guarantee code-share agreements. Under the terms of these code-share agreements, the major carrier controls marketing, scheduling, ticketing, pricing and seat inventories. We receive a guaranteed payment based upon a fixed minimum monthly amount plus amounts related to departures and block hours flown in addition to direct reimbursement of expenses such as fuel, landing fees and insurance. Among other advantages, revenue-guarantee arrangements reduce the Company s exposure to fluctuations in passenger traffic and fare levels, as well as fuel prices. The US Airways, Pre-Merger US Airways and Midwest Airlines Beechcraft 1900D turboprop code-share agreements are pro-rate agreements, for which we receive an allocated portion of each passenger s fare and pay all of the costs of transporting the passenger.

The following table summarizes our available seat miles (ASMs) flown and revenue recognized under our code-share agreements for the years ended September 30, 2006 and 2005:

	Fiscal 2006		Fiscal 2005	
	ASM s (000 s)	Passenger Revenue (000 s)	ASM s (000 s)	Passenger Revenue (000 s)

				(In thousands)					
US Airways (Revenue-Guarantee)	3,605,297	39%	$	609,232	47%	4,360,713	50%	$	487,221	44%
United (Revenue-Guarantee)	2,876,008	31%		477,151	36%	1,748,466	20%		260,541	24%
Pre-Merger US Airways (Revenue-Guarantee)	1,644,023	18%		58,511	4%	2,401,808	28%		316,072	29%
Delta (Revenue-Guarantee)	811,420	9%		121,315	9%					
US Airways (Pro-Rate)*	102,732	1%		24,821	2%	133,505	1%		30,126	2%
Mesa Airlines, Independent	55,552	1%		7,731	1%	71,257	1%		8,590	1%
go!	44,308			9,114	1%					
Total	9,139,340		$	1,307,875		8,715,749		$	1,102,550	

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* Amount includes the ASM s and Passenger Revenue associated with the Midwest Airlines (Pro-Rate) code-share agreement.

US Airways Code-Sharing Agreements

Revenue-Guarantee

As of September 30, 2006, we operated 38 CRJ-900, 18 CRJ-200, and six Dash-8 aircraft for US Airways under a revenue-guarantee code-share agreement. In exchange for providing flights and all other services under the agreement, we receive a fixed monthly minimum amount plus certain additional amounts based upon the number of flights flown and block hours performed during the month. US Airways also reimburses us for certain costs on an actual basis, including fuel costs, aircraft ownership and financing costs, landing fees, passenger liability and hull insurance, and aircraft property taxes, all as defined in the agreement. In addition, US Airways also provides, at no cost to Mesa, certain ground handling and customer service functions, as well as airport-related facilities and gates at US Airways hubs and cities where both carriers operate. We also receive a monthly payment from US Airways based on a percentage of revenue from flights that we operate under the code-share agreement. Under the amended code-share agreement, US Airways has the right to reduce the combined CRJ fleets utilized under the code-share agreement by one aircraft in any six-month period commencing in June 2006 (except during the calendar year 2007 in which 2 CRJ-200 can be eliminated in each six-month period). The Company has received notice of US Airways intent to reduce one CRJ-200 in December 2006, two CRJ-200s in April 2007 and two CRJ-200s in September 2007. In addition, beginning in February 2007, US Airways may eliminate the Dash-8 aircraft upon 180 days prior written notice. The code-share agreement terminates on June 30, 2012 unless US Airways elects to extend the contract for two years or exercises options to increase fleet size. The code-share agreement is subject to termination prior to that date in various circumstances including:

If our flight completion factor or arrival performance in the Phoenix Hub falls below a specified percentage for a specified period of time, subject to notice and cure rights;

If either US Airways or we become insolvent, file for bankruptcy or fail to pay our debts as they become due, the non-defaulting party may terminate the agreement;

Failure by us or US Airways to perform the covenants, conditions or provisions of the code-sharing agreement, subject to 15 days notice and cure rights;

If we or US Airways fail to make a payment when due, subject to ten business days notice and cure rights; or

If we are required by the FAA or the U.S. Department of Transportation (DOT) to suspend operations and we have not resumed operations within three business days, except as a result of an emergency airworthiness directive from the FAA affecting all similarly equipped aircraft, US Airways may terminate the agreement.

Pro-Rate

Pursuant to a turboprop code-share agreement with US Airways, we operated three Beechcraft 1900D turboprop aircraft primarily in Phoenix, Las Vegas and Salt Lake City under a pro-rate revenue-sharing arrangement as of September 30, 2006. We control scheduling, inventory and pricing. We are allocated a portion of each passenger s fare based on a standard industry formula and are required to pay all costs of transporting the passenger. The pro-rate agreement terminates on March 31, 2012 unless US Airways elects to extend the contract for successive one-year periods. The pro-rate agreement could also be terminated prior to the termination under similar circumstances as the revenue-guarantee agreement.

Pre-Merger US Airways Code-Sharing Agreement

Pro-Rate

Pursuant to a turboprop code-sharing agreement with Pre-Merger US Airways, we operated 13 Beechcraft 1900D turboprop aircraft under a pro-rate revenue-sharing arrangement as of September 30, 2006. We control scheduling, inventory and pricing subject to US Airways concurrence that such service does not adversely affect its other operations in the region. We are allocated a portion of each passenger s fare based on a standard industry formula and are required to pay all the costs of transporting the passenger. Additionally, we are required to pay certain franchise, marketing and reservation fees to US Airways.

US Airways may terminate the turboprop agreement at any time for cause upon not less than five days notice under any of the following conditions:

If we fail to utilize the aircraft as specified in the agreements.

If we fail to comply with the trademark license provisions of the agreement.

If we fail to perform the material terms, covenants or conditions of the code-sharing agreement.

Upon a change in our ownership or control without the written approval of US Airways.

The turboprop code-share agreement was scheduled to terminate in October 2006, but has been extended on its original terms as the Company and US Airways negotiate the terms of a new agreement. The Company expects to enter into a new agreement on substantially similar terms.

United Code-Sharing Agreement

As of September 30, 2006, we operated 37 CRJ-200, eight ERJ-145, 15 CRJ-700 (In October 2006, we added three additional CRJ-700s into service and removed three ERJ-145s from service) and ten Dash-8 aircraft for United under a code-sharing arrangement. The code-share agreement provides that we can increase our fleet to 45 50-seat and 30 CRJ-700 regional jet aircraft (15 of which would be replacements for 15 CRJ-200s). In exchange for performing the flight services under the agreement, we receive from United a fixed monthly minimum amount, plus certain additional amounts based upon the number of flights flown and block hours performed during the month. Additionally, certain costs incurred by us in performing the flight services are pass-through costs, whereby United agrees to reimburse us for the actual amounts incurred for these items: insurance, property tax per aircraft, fuel cost, oil cost, catering cost and landing fees. We also receive a profit margin based upon certain reimbursable costs under the agreement as well as our operational performance. The code-share agreement for (i) the ten Dash-8 aircraft terminates in July 2013 unless terminated by United by giving notice six months prior to April 30, 2010, (ii) the 15 50-seat CRJ-200s terminates no later than April 30, 2010, which can be accelerated up to two years at our discretion, (iii) the 30 50-seat regional jets terminates in July 2013, but can be terminated early in April 2010, (iv) the 15 CRJ-700s (to be delivered upon the withdrawal of the 50-seat regional jets) terminates ten years from delivery date, but no later than October 31, 2018, and (v) the remaining 15 CRJ-700s terminates in three tranches between December 31, 2011 and December 31, 2013. The code-share agreement is subject to termination prior to these dates under various circumstances including:

If certain operational performance factors fall below a specified percentage for a specified time, subject to notice and cure rights;

Failure by us to perform the material covenants, agreements, terms or conditions of the code-share agreement or similar agreements with United, subject to thirty (30) days notice and cure rights; or

If either United or we become insolvent, file bankruptcy or fail to pay debts when due, the non-defaulting party may terminate the agreement.

Delta Code-Sharing Agreement

As of September 30, 2006, we operated 28 ERJ-145 and six Dash-8 aircraft for Delta pursuant to two code-sharing agreements. Flight operations for Delta are performed by our wholly-owned subsidiary, Freedom Airlines. The regional jet and turboprop code-share agreements provide that we increase our fleet to 30 50-seat regional jet aircraft and 12 37-seat turboprop aircraft, respectively. In exchange for performing the flight services and our other obligations under the agreements, we receive from Delta monthly compensation made up of a fixed monthly amount, plus certain additional amounts based upon number of block hours flown and departures during the month. Additionally, certain costs incurred by Freedom are pass-through costs, whereby Delta agrees to reimburse us for the actual amounts incurred for these items: landing fees, hull insurance, passenger liability costs, fuel costs, catering costs and property taxes. Aircraft rent/ownership expenses are also considered a pass-through cost, but are limited to a specified amount for each type of aircraft. We are eligible to receive additional compensation based upon our completion rate and on-time arrival rate each month. Further, for each semi-annual period during the term of the agreement, we are eligible to receive additional compensation from Delta based upon performance. The fixed rates payable to us by Delta under the code-sharing agreement have been determined through the term of such agreement and are subject to annual revision.

The regional jet code-share agreement terminates on an aircraft-by-aircraft basis between 2017 and 2018. At the end of the term, Delta has the right to extend the agreement for additional one year successive terms on the same terms and conditions. Delta may terminate the code-sharing agreement at any time, with or without cause, upon twelve months prior written notice, provided such notice shall not be given prior to the earlier of (i) the sixth anniversary of the in-service date of the 30(th) aircraft added to the Delta Connection fleet by the Company, or (ii) November 2012. However, Delta has not yet assumed our regional jet code-share agreement in its bankruptcy proceedings and could choose to terminate this agreement at any time prior to its emergence from bankruptcy. In addition, according to news reports, US Airways, one of our code-share partners, has proposed to merge with Delta, another of our code-share partners. According to these same reports, Delta has rejected this proposal. We are unable, at this time, to predict what effect such a merger would have on our relationship with the parties or on our financial condition and operations. The turboprop agreement terminates in March 2009. At the end of the term, the turboprop agreement automatically renews for successive one-year terms on the same terms and conditions unless Delta provides us six months prior written notice of its intention to not renew. In addition, Delta may terminate the turboprop agreement, without cause, at any time after nine months after the Effective Date upon not less than six months prior written notice.

The agreements may be subject to early termination under various circumstances including:

- If either Delta or we file for bankruptcy, reorganization or similar action or if either Delta or we make an assignment for benefit of creditors;
- If either Delta or we commit a material breach of the code-share agreement, subject to 30 days notice and cure rights; or
- Upon the occurrence of an event of force majeure that continues for a period of 30 or more consecutive days.

In addition, Delta may immediately terminate the code-share agreement upon the occurrence of one or more of the following events:

- If there is a change of control of Freedom or Mesa;
- If there is a merger involving Freedom or Mesa;
- If we fail to maintain a specified completion rate with respect to the flights we operate for Delta during a specified period; or
- If our level of safety is not reasonably satisfactory to Delta.

Fleet Plans

CRJ Program

As of September 30, 2006, we operated 113 Canadair Regional Jets (60 CRJ-200/100, 15 CRJ-700 and 38 CRJ-900s).

In January 2004, we exercised options to purchase 20 CRJ-900 aircraft (seven of which can be converted to CRJ-700 aircraft). As of September 30, 2006, we have taken delivery of 13 CRJ-900 aircraft and two CRJ-700 aircraft. Subsequent to year end, we took delivery of a third CRJ-700 aircraft with two more CRJ-700 aircraft scheduled for delivery in March 2007. The delivery for the remaining two CRJ-900s (which can be converted to CRJ-700s) has not been finalized.

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ERJ Program

As of September 30, 2006, we operated 36 Embraer 145 aircraft. We acquired all 36 ERJ-145s through a June 1999 agreement with Empresa Brasiliera de Aeronautica S.A. (Embraer). We also have options for 25 additional aircraft. In September 2006, our contract with Embraer was amended to extend the option exercise date to August 2007 for deliveries beginning in January 2009.

Beechcraft 1900D

As of September 30, 2006, we owned 34 Beechcraft 1900D aircraft and were operating 20 of these aircraft. We lease four of our Beechcraft 1900D to Gulfstream International Airlines, a regional turboprop air carrier based in Ft. Lauderdale, Florida and lease an additional ten Beechcraft 1900D aircraft to Big Sky Transportation Co., a regional turboprop carrier based in Billings, Montana (Big Sky).

Dash-8

As of September 30, 2006, we operated 22 Dash-8 aircraft. In the fourth quarter of fiscal 2006, we took delivery of an additional four Dash-8 aircraft and placed them into revenue service during the first fiscal quarter of 2007.

Marketing

Our flight schedules are structured to facilitate the connection of our passengers with the flights of our code-share partners at their hub airports and to maximize local and connecting service to other carriers.

Under the Delta, United and US Airways revenue-guarantee code-share agreements, market selection, pricing and yield management functions are performed by our respective partners. The market selection process for our Beechcraft 1900D turboprop operations, outside the Essential Air Service program flights, includes an in-depth analysis on a route-by-route basis and is followed by a review and approval process in a joint effort with US Airways regarding the level of service and fares. We believe that this selection process enhances the likelihood of profitability in a given market. For our ***go!*** operations in Hawaii, we make all decisions on market selection, pricing and yield management functions.

Under our code-share agreements, the code-share partner coordinates advertising and public relations within their respective systems. In addition, our traffic is impacted by the major airline partners advertising programs in regions outside those served by us, with the major partners customers becoming our customers as a result of through fares. Under pro-rate code-share arrangements, our passengers also benefit from through fare ticketing with the major airline partners and greater accessibility to our flights on computer reservation systems and in the Official Airline Guide.

Our pro-rate agreements and independent flights are promoted through, and our revenues are generally believed to benefit from newspaper and radio promotions and advertisements, promotions on our websites www.iflygo.com and www.mesa-air.com, listings in computer reservation systems, the Official Airline Guide and through direct contact with travel agencies and corporate travel departments. Our independent operations utilize SABRE, a computerized reservation system widely used by travel agents, corporate travel offices and other airlines. The reservation systems of our code-share partners are also utilized in each of our other operations through their respective code-share agreements. We also pay booking fees to owners of other computerized reservation systems based on the number of independent and pro-rate passengers booked by travel agents using such systems.

Competition

The airline industry is highly competitive and volatile. Airlines compete in the areas of pricing, scheduling (frequency and timing of flights), on-time performance, type of equipment, cabin configuration, amenities provided to passengers, frequent flyer plans, and the automation of travel agent reservation systems. Further, because of the Airline Deregulation Act, airlines are currently free to set prices and establish new routes without the necessity of seeking governmental approval. At the same time, deregulation has allowed airlines to abandon unprofitable routes where the affected communities may be left without air service.

We believe that the Airline Deregulation Act facilitated our entry into scheduled air service markets and allows us to compete on the basis of service and fares, thus causing major carriers to seek out further contractual agreements with carriers like us as a way of expanding their respective networks. However, the Airline Deregulation Act makes the entry of other competitors possible, some of which may have substantial financial resources and experience, creating the potential for intense competition among regional air carriers in our markets.

Fuel

Historically, we have not experienced problems with the availability of fuel, and believe that we will be able to obtain fuel in quantities sufficient to meet our existing and anticipated future requirements at competitive prices. Standard industry contracts generally do not provide protection against fuel price increases, nor do they ensure availability of supply. However, our revenue-guarantee code-share agreements with Delta, United and US Airways (regional jet) allow fuel used in the performance of the agreements to be reimbursed by our code-share partner, thereby reducing our exposure to fuel price fluctuations. In fiscal 2006, approximately 96% of our fuel purchases was associated with our Delta, United and US Airways (regional jet) and Pre-Merger US Airways revenue-guarantee code-share agreements. A substantial increase in the price of jet fuel, to the extent our fuel costs are not reimbursed, or the lack of adequate fuel supplies in the future, could have a material adverse effect on our business, financial condition, results of operations and liquidity.

Maintenance of Aircraft and Training

All mechanics and avionics specialists employed by us have the appropriate training and experience and hold the required licenses issued by the FAA. Using a combination of FAA-certified maintenance vendors and our own personnel and facilities, we maintain our aircraft on a scheduled and as-needed basis. We emphasize preventive maintenance and inspect our aircraft engines and airframes as required. We also maintain an inventory of spare parts specific to the aircraft types we fly. We provide periodic in-house and outside training for our maintenance and flight personnel and also take advantage of factory training programs that are offered when acquiring new aircraft.

Insurance

We carry types and amounts of insurance customary in the regional airline industry, including coverage for public liability, passenger liability, property damage, product liability, aircraft loss or damage, baggage and cargo liability and workers compensation.

As a result of the terrorist attacks on September 11, 2001, aviation insurers have significantly reduced the maximum amount of insurance coverage available to commercial air carriers for war-risk (terrorism) coverage, while at the same time, significantly increasing the premiums for this coverage as well as for aviation insurance in general. Given the significant increase in insurance costs, the federal government is currently providing insurance assistance under the Air Transportation Safety and System Stabilization Act. In addition, the federal government has issued war-risk coverage to U.S. air carriers that is generally renewable for 60-day periods. However, the availability of aviation insurance is not guaranteed and our inability to obtain such coverage at affordable rates may result in the grounding of our aircraft. Insurance costs are reimbursed under the terms of our revenue-guarantee code-share agreements.

Employees

As of September 30, 2006, we employed approximately 5,200 employees. Approximately 3,000 of our employees are represented by various labor organizations. Our continued success is partly dependent on our ability to continue to attract and retain qualified personnel. Historically, we have had no difficulty attracting qualified personnel to meet our requirements.

Relations between air carriers and labor unions in the United States are governed by the Railway Labor Act or RLA. Under the RLA, collective bargaining agreements generally contain amendable dates rather than expiration dates, and the RLA requires that a carrier maintain the existing terms and conditions of employment following the amendable date through a multi-stage and usually lengthy series of bargaining processes overseen by the National Mediation Board. Mesa Airline s and Freedom Airline s flight attendants are represented by the Association of

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Flight Attendants (AFA). Both contracts covering flight attendants became amendable in June 2006 and the Company is in the early stages of negotiations with its flight attendants. The pilots of Mesa Airlines, Freedom Airlines and Air Midwest are collectively represented under a single contract by the Air Line Pilot Association (ALPA). Our contract with ALPA becomes amendable in September 2007.

Although not currently observing high turnover, pilot turnover at times is a significant issue among regional carriers when major carriers are hiring experienced commercial pilots away from regional carriers. The addition of aircraft, especially new aircraft types, can result in pilots upgrading between aircraft types and becoming unavailable for duty during the extensive training periods required. No assurances can be made that pilot turnover and unavailability will not be a significant problem in the future, particularly if major carriers expand their operations. Similarly, there can be no assurance that sufficient numbers of new pilots will be available to support any future growth.

No other Mesa subsidiaries are parties to any other collective bargaining agreement or union contracts.

Essential Air Service Program

The Essential Air Service (EAS) program administered by the DOT guarantees a minimum level of air service in certain communities, predicated on predetermined guidelines set forth by Congress. Based on these guidelines, the DOT subsidizes air service to communities that might not otherwise have air service. At September 30, 2006, we provided service to 30 such cities for an annualized subsidy of approximately $21 million. EAS rates are normally set for two-year contract periods for each city. There is no guarantee that we will continue to receive subsidies for the cities we serve. The DOT may request competitive proposals from other airlines at the end of the contract period for EAS service to a particular city. Proposals, when requested, are evaluated on, among other things, level of service provided, subsidy requested, fitness of the applicant and comments from the communities served. If the funding under this program is terminated for any of the cities served by us, in all likelihood we would not continue to fly in these markets, and as a result, we would be forced to find alternative uses for the Beechcraft 1900D 19-seat turboprop aircraft affected.

Investment Activities

In fiscal 2006, we participated with a private equity fund in making an investment in the common stock and notes of a closely held airline related business (the Investee). Through our subsidiary Nilchii, we invested $15 million, which represents approximately 20% and 11.8% of the Investee s common stock and notes, respectively.

Regulation

As an interstate air carrier, we are subject to the economic jurisdiction, regulation and continuing air carrier fitness requirements of the DOT. Such requirements include minimum levels of financial, managerial and regulatory fitness. The DOT is authorized to establish consumer protection regulations to prevent unfair methods of competition and deceptive practices, to prohibit certain pricing practices, to inspect a carrier s books, properties and records, and to mandate conditions of carriage. The DOT also has the power to bring proceedings for the enforcement of air carrier economic regulations, including the assessment of civil penalties, and to seek criminal sanctions.

We are subject to the jurisdiction of the FAA with respect to our aircraft maintenance and operations, including equipment, ground facilities, dispatch, communication, training, weather observation, flight personnel and other matters affecting air safety. To ensure compliance with its regulations, the FAA requires airlines to obtain an operating certificate, which is subject to suspension or revocation for cause, and provides for regular inspections.

We are subject to various federal and local laws and regulations pertaining to other issues of environmental protocol. We believe we are in compliance with all governmental laws and regulations regarding environmental protection.

We are also subject to the jurisdiction of the Federal Communications Commission with respect to the use of our radio facilities and the United States Postal Service with respect to carriage of United States mail.

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Local governments in certain markets have adopted regulations governing various aspects of aircraft operations, including noise abatement and curfews.

Available Information

We maintain a website where additional information concerning our business can be found. The address of that website is *www.mesa-air.com. We make available free of charge on our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, as soon as reasonably practicable after we electronically file or furnish such materials to the SEC.*

Item 1A. *Risk Factors*

The following risk factors, in addition to the information discussed elsewhere herein, should be carefully considered in evaluating us and our business:

Risks Related to Our Business

We are dependent on our agreements with our code-share partners.

We depend on relationships created by our code-share agreements. We derive a significant portion of our consolidated passenger revenues from our revenue-guarantee code-share agreements with Delta Air Lines, United Airlines and US Airways. Our code-share partners have certain rights to cancel the applicable code-share agreement upon the occurrence of certain events or the giving of appropriate notice, subject to certain conditions. No assurance can be given that one or more of our code-share partners will not serve notice at a later date of their intention to cancel our code-sharing agreement, forcing us to stop selling those routes with the applicable partner s code and potentially reducing our traffic and revenue.

Our code-share agreement with US Airways allows US Airways, subject to certain restrictions, to reduce the combined CRJ fleets utilized under the code-share agreement by one aircraft in any six-month period commencing in June 2006 (except during the calendar year 2007 in which 2 CRJ-200 can be eliminated in each six-month period). In addition, beginning in February 2007, US Airways may eliminate the Dash-8 aircraft upon 180 days prior written notice. US Airways has notified the Company of its intent to reduce the maximum number of CRJs in 2006 and 2007. US Airways has used this provision to reduce the number of aircraft covered by the code-share agreement and we anticipate they will continue to further reduce the number of covered aircraft in accordance with the agreement.

In addition, because a majority of our operating revenues are currently generated under revenue-guarantee code-share agreements, if any one of them is terminated, our operating revenues and net income could be materially adversely affected unless we are able to enter into satisfactory substitute arrangements or, alternatively, fly under our own flight designator code, including obtaining the airport facilities and gates necessary to do so. For the year ended September 30, 2006, our US Airways revenue-guarantee code-share agreement accounted for 51% of our consolidated passenger revenues, our Delta code-share agreement accounted for 9% of our consolidated passenger revenue and our United code-share agreement accounted for 36% of our consolidated passenger revenues.

If our code-share partners or other regional carriers experience events that negatively impact their financial strength or operations, our operations also may be negatively impacted.

We are directly affected by the financial and operating strength of our code-share partners. Any events that negatively impact the financial strength of our code-share partners or have a long-term effect on the use of our code-share partners by airline travelers would likely have a material adverse effect on our business, financial condition and results of operations. In the event of a decrease in the financial or operational strength of any of our code-share partners, such partner may seek to reduce, or be unable to make, the payments due to us under their code-share agreement. In addition, they may reduce utilization of our aircraft. Although there are certain monthly guaranteed payment amounts, there are no minimum levels of utilization specified in the code-share agreements. Delta has not yet assumed our code-share agreement in its bankruptcy proceeding and could choose to terminate this agreement or seek to renegotiate the agreement on terms less favorable to us. If any of our other current or future code-share

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partners become bankrupt, our code-share agreement with such partner may not be assumed in bankruptcy and would be terminated. This and other such events could have a material adverse effect on our business, financial condition and results of operations. In addition, any negative events that occur to other regional carriers and that affect public perception of such carriers generally could also have a material adverse effect on our business, financial condition and results of operations.

Our code-share partners may expand their direct operation of regional jets thus limiting the expansion of our relationships with them.

We depend on major airlines like Delta, United Airlines and US Airways electing to contract with us instead of purchasing and operating their own regional jets. However, these major airlines possess the resources to acquire and operate their own regional jets instead of entering into contracts with us or other regional carriers. We have no guarantee that in the future our code-share partners will choose to enter into contracts with us instead of purchasing their own regional jets or entering into relationships with competing regional airlines. A decision by Delta, United Airlines, or US Airways to phase out our contract-based code-share relationships or to enter into similar agreements with competitors could have a material adverse effect on our business, financial condition or results of operations. In addition to Mesa, our partners have similar code-share agreements with other competing regional airlines. According to news reports, US Airways, one of our code-share partners, has proposed to merge with Delta, another of our code-share partners. According to these same reports, Delta has rejected this proposal. We are unable, at this time, to predict what effect such a merger would have on our relationship with the parties or on our financial condition and operations.

If we experience a lack of labor availability or strikes, it could result in a decrease of revenues due to the cancellation of flights.

The operation of our business is significantly dependent on the availability of qualified employees, including, specifically, flight crews, mechanics and avionics specialists. Historically, regional airlines have periodically experienced high pilot turnover as a result of air carriers operating larger aircraft hiring their commercial pilots. Further, the addition of aircraft, especially new aircraft types, can result in pilots upgrading between aircraft types and becoming unavailable for duty during the required extensive training periods. There can be no assurance that we will be able to maintain an adequate supply of qualified personnel or that labor expenses will not increase.

At September 30, 2006, we had approximately 5,200 employees, approximately 3,000 of whom are members of labor unions, including ALPA and the AFA. Our collective bargaining agreement with ALPA becomes amendable in September 2007 and our collective bargaining agreement with the AFA became amendable in June 2006 and the Company is in the early stages of negotiations with its flight attendants. The inability to negotiate acceptable contracts with existing unions as agreements expire or with new unions could result in work stoppages by the affected workers, lost revenues resulting from the cancellation of flights and increased operating costs as a result of higher wages or benefits paid to union members. We cannot predict which, if any, other employee groups may seek union representation or the outcome or the terms of any future collective bargaining agreement and therefore the effect, if any, on our business financial condition and results of operations. If negotiations with unions over collective bargaining agreements prove to be unsuccessful, following specified cooling off periods, the unions may initiate a work action, including a strike, which could have a material adverse effect on our business, financial condition and results of operations.

Increases in our labor costs, which constitute a substantial portion of our total operating costs, will cause our earnings to decrease.

Labor costs constitute a significant percentage of our total operating costs. Under our code-share agreements, our reimbursement rates contemplate labor costs that increase on a set schedule generally tied to an increase in the consumer price index or the actual increase in the contract. We are responsible for our labor costs, and we may not be entitled to receive increased payments under our code-share agreements if our labor costs increase above the assumed costs included in the reimbursement rates. As a result, a significant increase in our labor costs above the levels assumed in our reimbursement rates could result in a material reduction in our earnings.

If new airline regulations are passed or are imposed upon our operations, we may incur increased operating costs and experience a decrease in earnings.

Laws and regulations, such as those described below, have been proposed from time to time that could significantly increase the cost of our operations by imposing additional requirements or restrictions on our operations. We cannot predict what laws and regulations will be adopted or what changes to air transportation agreements will be effected, if any, or how they will affect us, and there can be no assurance that laws or regulations currently proposed or enacted in the future will not increase our operating expenses and therefore adversely affect our financial condition and results of operations.

As an interstate air carrier, we are subject to the economic jurisdiction, regulation and continuing air carrier fitness requirements of the DOT, which include required levels of financial, managerial and regulatory fitness. The DOT is authorized to establish consumer protection regulations to prevent unfair methods of competition and deceptive practices, to prohibit certain pricing practices, to inspect a carrier s books, properties and records, to mandate conditions of carriage and to suspend an air carrier s fitness to operate. The DOT also has the power to bring proceedings for the enforcement of air carrier economic regulations, including the assessment of civil penalties, and to seek criminal sanctions.

We are also subject to the jurisdiction of the FAA with respect to our aircraft maintenance and operations, including equipment, ground facilities, dispatch, communication, training, weather observation, flight personnel and other matters affecting air safety. To ensure compliance with its regulations, the FAA requires airlines to obtain an operating certificate, which is subject to suspension or revocation for cause, and provides for regular inspections.

We incur substantial costs in maintaining our current certifications and otherwise complying with the laws, rules and regulations to which we are subject. We cannot predict whether we will be able to comply with all present and future laws, rules, regulations and certification requirements or that the cost of continued compliance will not significantly increase our costs of doing business.

The FAA has the authority to issue mandatory orders relating to, among other things, the grounding of aircraft, inspection of aircraft, installation of new safety-related items and removal and replacement of aircraft parts that have failed or may fail in the future. A decision by the FAA to ground, or require time-consuming inspections of, or maintenance on, all or any of our turboprops or regional jets, for any reason, could negatively impact our results of operations.

In addition to state and federal regulation, airports and municipalities enact rules and regulations that affect our operations. From time to time, various airports throughout the country have considered limiting the use of smaller aircraft, such as Embraer or Canadair regional jets, at such airports. The imposition of any limits on the use of our regional jets at any airport at which we operate could interfere with our obligations under our code-share agreements and severely interrupt our business operations.

lf additional security and safety measures regulations are adopted, we may incur increased operating costs and experience a decrease in earnings.

Congress has adopted increased safety and security measures designed to increase airline passenger security and protect against terrorist acts. Such measures have resulted in additional operating costs to the airline industry. The Aviation Safety Commission s report recommends the adoption of further measures aimed at improving the safety and security of air travel. We cannot forecast what additional security and safety requirements may be imposed on our operations in the future or the costs or revenue impact that would be associated with complying with such requirements, although such costs and revenue impact could be significant. To the extent that the costs of complying with any additional safety and security measures are not reimbursed by our code-share partners, our operating results and net income could be adversely affected.

If our operating costs increase as our aircraft fleet ages and we are unable to pass along such costs, our earnings will decrease.

As our fleet of aircraft age, the cost of maintaining such aircraft, if not replaced, will likely increase. There can be no assurance that costs of maintenance, including costs to comply with aging aircraft requirements, will not materially increase in the future. Any material increase in such costs could have a material adverse effect on our business, financial condition and results of operations. Because many aircraft components are required to be replaced after specified numbers of flight hours or take-off and landing cycles, and because new aviation technology may be required to be retrofitted, the cost to maintain aging aircraft will generally exceed the cost to maintain newer aircraft. We believe that the cost to maintain our aircraft in the long-term will be consistent with industry experience for these aircraft types and ages used by comparable airlines.

We believe that our aircraft are mechanically reliable based on the percentage of scheduled flights completed and as of September 30, 2006 the average age of our regional jet fleet is 4.0 years. However, there can be no assurance that such aircraft will continue to be sufficiently reliable over longer periods of time. Furthermore, any public perception that our aircraft are less than completely reliable could have a material adverse effect on our business, financial condition and results of operations.

Our fleet expansion program has required a significant increase in our leverage.

The airline business is very capital intensive and we are highly leveraged. For the year ended September 30, 2006, our debt service payments, including principal and interest, totaled $73.3 million and our aircraft lease payments totaled $246.8 million. We have significant lease obligations with respect to our aircraft and ground facilities, which aggregated approximately $2.3 billion at September 30, 2006. As of September 30, 2006, our growth strategy involves the acquisition of three more Bombardier regional jets during fiscal 2007. As of September 30, 2006, we had permanently financed all but five CRJ-700 and CRJ-900 aircraft delivered under the 2001 BRAD agreement. We may utilize interim financing provided by the manufacturer and have the ability to fund up to 15 aircraft at any one time under this facility. There are no assurances that we will be able to obtain permanent financing for future aircraft deliveries.

There can be no assurance that our operations will generate sufficient cash flow to make such payments or that we will be able to obtain financing to acquire the additional aircraft necessary for our expansion. If we default under our loan or lease agreements, the lender/lessor has available extensive remedies, including, without limitation, repossession of the respective aircraft and, in the case of large creditors, the effective ability to exert control over how we allocate a significant portion of our revenues. Even if we are able to timely service our debt, the size of our long-term debt and lease obligations could negatively affect our financial condition, results of operations and the price of our common stock in many ways, including:

- increasing the cost, or limiting the availability of, additional financing for working capital, acquisitions or other purposes;
- limiting the ways in which we can use our cash flow, much of which may have to be used to satisfy debt and lease obligations; and
- adversely affecting our ability to respond to changing business or economic conditions or continue our growth strategy.

Reduced utilization levels of our aircraft under the revenue-guarantee agreements would adversely impact our revenues and earnings.

Even though our revenue-guarantee agreements require a fixed amount per month to compensate us for our fixed costs, if our aircraft are underutilized (including taking into account the stage length and frequency of our scheduled flights) we will lose the opportunity to receive a margin on the variable costs of flights that would have been flown if our aircraft were more fully utilized.

If we incur problems with any of our third-party service providers, our operations could be adversely affected by a resulting decline in revenue or negative public perception about our services.

Our reliance upon others to provide essential services on behalf of our operations may result in the relative inability to control the efficiency and timeliness of contract services. We have entered into agreements with contractors to provide various facilities and services required for our operations, including aircraft maintenance, ground facilities, baggage handling and personnel training. It is likely that similar agreements will be entered into in any new markets we decide to serve. All of these agreements are subject to termination after notice. Any material problems with the efficiency and timeliness of contract services could have a material adverse effect on our business, financial condition and results of operations.

We are at risk of loss and adverse publicity stemming from any accident involving any of our aircraft.

If one of our aircraft were to crash or be involved in an accident, we could be exposed to significant tort liability.

There can be no assurance that the insurance we carry to cover damages arising from any future accidents will be adequate. Accidents could also result in unforeseen mechanical and maintenance costs. In addition, any accident involving an aircraft that we operate could create a public perception that our aircraft are not safe, which could result in air travelers being reluctant to fly on our aircraft. To the extent a decrease in air travelers is associated with our operations not covered by our code-share agreements, such a decrease could have a material adverse affect on our business, financial condition or results of operations.

If we become involved in any material litigation or any existing litigation is concluded in a manner adverse to us, our earnings may decline.

We are, from time to time, subject to various legal proceedings and claims, either asserted or unasserted. Any such claims, whether with or without merit, could be time-consuming and expensive to defend and could divert management s attention and resources. There can be no assurance regarding the outcome of current or future litigation.

In February 2006, Hawaiian Airlines, Inc. (Hawaiian) filed a complaint against the Company in the United States Bankruptcy Court for the District of Hawaii (the Bankruptcy Court) alleging that the Company breached the terms of a Confidentiality Agreement entered into in April 2004 with the Trustee in Hawaiian s bankruptcy proceedings. Hawaiian s complaint alleges, among other things, that the Company breached the Confidentiality Agreement by (a) using the evaluation material to obtain a competitive advantage over Hawaiian, through the development and implementation of a business plan to compete with Hawaiian in the inter-island market, and (b) failing to return or destroy any evaluation materials after being notified by Hawaiian on or about May 12, 2004 that the Company had not been selected as a potential investor for a transaction with Hawaiian. Hawaiian, in its complaint, seeks unspecified damages, requests that the Company turn over to Hawaiian any evaluation material in the Company s possession, custody or control (the Turnover Claim), and an injunction preventing the Company from providing inter-island transportation services in the State of Hawaii for a period of two years from the date of such injunctive relief.

The Company vigorously denies Hawaiian s allegations and requests for relief contained in its complaint. The Company filed both an answer and an antitrust counterclaim against Hawaiian in response to its complaint. In May 2006, the Company filed a motion to dismiss the Turnover Claim contained in Hawaiian s complaint, but the Bankruptcy Court denied that motion. On December 8, 2006 the Bankruptcy Court, based on constitutional access to the courts, also granted Hawaiian s motion for summary judgment against the Company on its antitrust counterclaim. The Company does not believe that either of these decisions has a material impact on the Company s position in the lawsuit. Finally, in October 2006, the Bankruptcy Court denied Hawaiian s effort to enjoin the Company s ***go!*** operation from selling tickets claiming that ***go!*** s entry into the inter-island air transport business was based on trade secrets furnished to Mesa during the Hawaiian bankruptcy. The Court found no such misuse of confidential information and rejected Hawaiian s motion for a preliminary injunction.

In June 2006, Hawaiian requested a preliminary injunction to prevent the Company from issuing new airline tickets for the Hawaiian inter-island market for a period of one year. In this request, Hawaiian alleges that initial discovery conducted reveals that the Company breached the Confidentiality Agreement. The Court has recently denied Hawaiian s request for a preliminary injunction. The case will be tried sometime in 2007.

On October 13, 2006, Aloha Airlines filed suit against Mesa Air Group and two of its Hawaii based employees, Charles Lauritsen, ***go!*** s Chief Operating Officer and Joe Bock, ***go!*** s Chief Marketing Officer. The complaint was filed in state court in Hawaii and contains 11 counts and seeks damages and injunctive relief. The clear purpose of

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the complaint is to blunt Mesa s entry into the Hawaii inter-island market segment. Aloha alleges that Mesa s inter-island air fares are below cost and that Mesa is, therefore, violating specific provisions of Hawaii antitrust and unfair competition law. Aloha also alleges breach of contract and fraud by Mesa in connection with two confidentiality agreements, one in 2005 and the other in 2006.

In 1992, The Supreme Court of the United States decided Morales v. TWA, in which it construed the Airline Deregulation Act as prohibiting any state court, under any state law legal theory, from adjudicating issues which implicated an air carrier s pricing (or other service) practices. Accordingly, an airline s pricing decisions can be attacked only under federal laws. In response to the complaint, Mesa filed a motion on December 8 seeking dismissal of all claims which rest on Mesa s alleged below-cost pricing.

Mesa also denies any improper use of the data furnished by Aloha while Mesa was considering a bid for Aloha during its bankruptcy. The case is in its incipient stages and no trial date has yet been set.

Our business would be harmed if we lose the services of our key personnel.

Our success depends to a large extent on the continued service of our executive management team. We have employment agreements with certain executive officers, but it is possible that members of executive management may leave us. Departures by our executive officers could have a negative impact on our business, as we may not be able to find suitable management personnel to replace departing executives on a timely basis. We do not maintain key-man life insurance on any of our executive officers.

We may experience difficulty finding, training and retaining employees.

Our business is labor intensive, we require large numbers of pilots, flight attendants, maintenance technicians and other personnel. The airline industry has from time to time experienced a shortage of qualified personnel, specifically pilots and maintenance technicians. In addition, as is common with most of our competitors, we have faced considerable turnover of our employees. Although our employee turnover has decreased significantly since September 11, 2001, our pilots, flight attendants and maintenance technicians often leave to work for larger airlines, which generally offer higher salaries and better benefit programs than regional airlines are financially able to offer. Should the turnover of employees, particularly pilots and maintenance technicians, sharply increase, the result will be significantly higher training costs than otherwise would be necessary. We cannot assure you that we will be able to recruit, train and retain the qualified employees that we need to carry out our expansion plans or replace departing employees. If we are unable to hire and retain qualified employees at a reasonable cost, we may be unable to complete our expansion plans, which could have a material adverse effect on our financial condition, results of operations and the price of our common stock.

We may be unable to profitably operate our Hawaiian airline, which could negatively impact our business and operations.

In June 2006, we launched our independent inter-island Hawaiian airline operation named ***go!*** Providing service in Hawaii will require ongoing investment of working capital by Mesa and management attention and focus.

Further, in light of the costs and risks associated with operating an independent low fare regional jet airline, we may be unable to operate the Hawaiian airline profitably, which would negatively impact our business, financial condition and results of operations.

In addition, our results under our revenue-guarantee contracts offer no meaningful guidance with respect to our future performance in running an independent airline because we have not previously operated as an independent regional jet carrier in Hawaii. We are operating under a new brand that will initially have limited market recognition. Future performance will depend on a number of factors, including our ability to:

establish a brand that is attractive to our target customers;

maintain adequate controls over our expenses;

monitor and manage operational and financial risks;

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secure favorable terms with airports, suppliers and other contractors;

maintain the safety and security of our operations;

attract, retain and motivate qualified personnel; and

react to responses from competitors who are more established in the Hawaiian markets.

Risks Related to Our Industry

If competition in the airline industry increases, we may experience a decline in revenue.

Increased competition in the airline industry as well as competitive pressure on our code-share partners or in our markets could have a material adverse effect on our business, financial condition and results of operation. The airline industry is highly competitive. The earnings of many of the airlines have historically been volatile. The airline industry is susceptible to price discounting, which involves the offering of discount or promotional fares to passengers. Any such fares offered by one airline are normally matched by competing airlines, which may result in lower revenue per passenger, i.e., lower yields, without a corresponding increase in traffic levels. Also, in recent years several new carriers have entered the industry, typically with low cost structures. In some cases, new entrants have initiated or triggered price discounting. The entry of additional new major or regional carriers in any of our markets, as well as increased competition from or the introduction of new services by established carriers, could negatively impact our financial condition and results of operations.

Our reliance on our code-share agreements with our major airline partners for the majority of our revenue means that we must rely on the ability of our code-share partners to adequately promote their respective services and to maintain their respective market share. Competitive pressures by low-fare carriers and price discounting among major airlines could have a material adverse effect on our code-share partners and therefore adversely affect our business, financial condition and results of operations.

The results of operations in the air travel business historically fluctuate in response to general economic conditions. The airline industry is sensitive to changes in economic conditions that affect business and leisure travel and is highly susceptible to unforeseen events, such as political instability, regional hostilities, economic recession, fuel price increases, inflation, adverse weather conditions or other adverse occurrences that result in a decline in air travel. Any event that results in decreased travel or increased competition among airlines could have a material adverse effect on our business, financial condition and results of operations.

In addition to traditional competition among airlines, the industry faces competition from ground and sea transportation alternatives. Video teleconferencing and other methods of electronic communication may add a new dimension of competition to the industry as business travelers seek lower-cost substitutes for air travel.

The airline industry is heavily regulated.

Airlines are subject to extensive regulatory and legal compliance requirements, both domestically and internationally, that involve significant costs. In the last several years, the FAA has issued a number of directives and other regulations relating to the maintenance and operation of aircraft that have required us to make significant expenditures. FAA requirements cover, among other things, retirement of older aircraft, security measures, collision avoidance systems, airborne wind shear avoidance systems, noise abatement, commuter aircraft safety and increased inspection and maintenance procedures to be conducted on older aircraft.

We incur substantial costs in maintaining our current certifications and otherwise complying with the laws, rules and regulations to which we are subject. We cannot predict whether we will be able to comply with all present and future laws, rules, regulations and certification requirements or that the cost of continued compliance will not significantly increase our costs of doing business, to the extent such costs are not reimbursed by our code-share partners.

The FAA has the authority to issue mandatory orders relating to, among other things, the grounding of aircraft, inspection of aircraft, installation of new safety-related items and removal and replacement of aircraft parts that

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have failed or may fail in the future. A decision by the FAA to ground, or require time consuming inspections of or maintenance on, all or any of our aircraft, for any reason, could negatively impact our results of operations.

In addition to state and federal regulation, airports and municipalities enact rules and regulations that affect our operations. From time to time, various airports throughout the country have considered limiting the use of smaller aircraft at such airports. The imposition of any limits on the use of our aircraft at any airport at which we operate could interfere with our obligations under our code-share agreements and severely interrupt our business operations.

Additional laws, regulations, taxes and airport rates and charges have been proposed from time to time that could significantly increase the cost of airline operations or reduce revenues. If adopted, these measures could have had the effect of raising ticket prices, reducing revenue and increasing costs. In addition, as a result of the terrorist attacks in New York and Washington, D.C. in September 2001, the FAA has imposed more stringent security procedures on airlines and imposed security taxes on each ticket sold. We cannot predict what other new regulations may be imposed on airlines and we cannot assure you that laws or regulations enacted in the future will not materially adversely affect our financial condition, results of operations and the price of our common stock.

The airline industry has been subject to a number of strikes which could affect our business.

The airline industry has been negatively impacted by a number of labor strikes. Any new collective bargaining agreement entered into by other regional carriers may result in higher industry wages and add increased pressure on us to increase the wages and benefits of our employees. Furthermore, since each of our code-share partners is a significant source of revenue, any labor disruption or labor strike by the employees of any one of our code-share partners could have a material adverse effect on our financial condition, results of operations and the price of our common stock.

Risks Related to Our Common Stock

Provisions in our charter documents might deter acquisition bids for us.

Our articles of incorporation and bylaws contain provisions that, among other things:

- authorize our board of directors to issue preferred stock ranking senior to our common stock without any action on the part of the shareholders;
- establish advance notice procedures for shareholder proposals, including nominations of directors, to be considered at shareholders meetings;
- authorize a majority of our board of directors, in certain circumstances, to fill vacancies on the board resulting from an increase in the authorized number of directors or from vacancies;
- restrict the ability of shareholders to modify the number of authorized directors; and
- restrict the ability of stockholders to call special meetings of shareholders.

In addition, Section 78.438 of the Nevada general corporation law prohibits us from entering into some business combinations with interested stockholders without the approval of our board of directors. These provisions could make it more difficult for a third party to acquire us, even if doing so would benefit our stockholders.

Our stock price may continue to be volatile and could decline substantially.

The stock market has, from time to time, experienced extreme price and volume fluctuations. Many factors may cause the market price for our common stock to decline following this Form 10-K, including:

- our operating results failing to meet the expectations of securities analysts or investors in any quarter;
- downward revisions in securities analysts estimates;
- material announcements by us or our competitors;
- public sales of a substantial number of shares of our common stock following this Form 10-K;

governmental regulatory action; or

adverse changes in general market conditions or economic trends.

Item 1B. ***Unresolved Staff Comments***

None.

Item 2. ***Properties***

Our primary property consists of the aircraft used in the operation of our flights. The following table lists the aircraft owned and leased by the Company as of September 30, 2006.

	Number of Aircraft					
Type of Aircraft	**Owned**	**Interim Financing**	**Leased**	**Total**	**Operating on Sept. 30, 2006**	**Passenger Capacity**
CRJ-200/100 Regional Jet	2		58	60	60	50
CRJ-700 Regional Jet	5	2	10	17	15	66
CRJ-900 Regional Jet	11	3	24	38	38	86
Embraer 145 Regional Jet			36	36	36	50
Beechcraft 1900D	34			34	20	19
Dash-8			28	28	22	37
Embraer EMB-120			2	2		30
Total	52	5	158	215	191	

See Business Airline Operations and MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS Liquidity and Capital Resources for a discussion regarding the Company s aircraft fleet commitments.

In addition to aircraft, we have office and maintenance facilities to support our operations. Our facilities are summarized in the following table:

Type	**Location**	**Ownership**	**Approximate Square Feet**
Headquarters	Phoenix, AZ	Leased	36,000
Training/Administration	Phoenix, AZ	Leased	27,000
Hangar/Office	Phoenix, AZ	Leased	22,000
Engine Shop & Commissary	Phoenix, AZ	Leased	25,000
RAS Office/Component Overhaul Facility	Phoenix, AZ	Leased	19,000
Customer Service Training/Storage	Phoenix, AZ	Leased	10,000

Office (East Coast)	Charlotte, NC	Leased	5,500
Hangar	Charlotte, NC	Leased	30,000
Hangar	Columbia, SC	(1)	20,000
Hangar	Columbia, SC	(1)	35,350
Hangar	Grand Junction, CO	(1)	25,000
Hangar/Office	Wichita, KS	(1)	20,000
Training/Administration	Farmington, NM	(1)	10,000
Hangar	Farmington, NM	(1)	24,000
Hangar/Office	Dubois, PA	(1)	23,000
Hangar	Orlando, FL	Leased	18,693
Office	Honolulu, HI	Leased	7,793

(1) Building is owned, underlying land is leased.

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We lease ticket counters, check-in and boarding and other facilities in the passenger terminal areas in the majority of the airports we serve and staff those facilities with our personnel. Delta, United and US Airways also provide facilities, ticket handling and ground support services for us at certain airports.

Our corporate headquarters and training/administrative facilities in Phoenix, Arizona are subject to long-term leases expiring on August 31, 2012 and November 1, 2012, respectively.

We believe our facilities are suitable and adequate for our current and anticipated needs.

Item 3. *Legal Proceedings*

In February 2006, Hawaiian Airlines, Inc. (Hawaiian) filed a complaint against the Company in the United States Bankruptcy Court for the District of Hawaii (the Bankruptcy Court) alleging that the Company breached the terms of a Confidentiality Agreement entered into in April 2004 with the Trustee in Hawaiian s bankruptcy proceedings. Hawaiian s complaint alleges, among other things, that the Company breached the Confidentiality Agreement by (a) using the evaluation material to obtain a competitive advantage over Hawaiian, through the development and implementation of a business plan to compete with Hawaiian in the inter-island market, and (b) failing to return or destroy any evaluation materials after being notified by Hawaiian on or about May 12, 2004 that the Company had not been selected as a potential investor for a transaction with Hawaiian. Hawaiian, in its complaint, seeks unspecified damages, requests that the Company turn over to Hawaiian any evaluation material in the Company s possession, custody or control (the Turnover Claim), and an injunction preventing the Company from providing inter-island transportation services in the State of Hawaii for a period of two years from the date of such injunctive relief.

The Company vigorously denies Hawaiian s allegations and requests for relief contained in its complaint. The Company filed both an answer and an antitrust counterclaim against Hawaiian in response to its complaint. In May 2006, the Company filed a motion to dismiss the Turnover Claim contained in Hawaiian s complaint, but the Bankruptcy Court denied that motion. On December 8, 2006 the Bankruptcy Court, based on constitutional access to the courts, also granted Hawaiian s motion for summary judgment against the Company on its antitrust counterclaim. The Company does not believe that either of these decisions has a material impact on the Company s position in the lawsuit. Finally, in October 2006, the Bankruptcy Court denied Hawaiian s effort to enjoin the Company s ***go!*** operation from selling tickets claiming that ***go!*** s entry into the inter-island air transport business was based on trade secrets furnished to Mesa during the Hawaiian bankruptcy. The Court found no such misuse of confidential information and rejected Hawaiian s motion for a preliminary injunction.

In June 2006, Hawaiian requested a preliminary injunction to prevent the Company from issuing new airline tickets for the Hawaiian inter-island market for a period of one year. In this request, Hawaiian alleges that initial discovery conducted reveals that the Company breached the Confidentiality Agreement. The Court has recently denied Hawaiian s request for a preliminary injunction. The case will be tried sometime in 2007.

On October 13, 2006, Aloha Airlines filed suit against Mesa Air Group and two if its Hawaii based employees, Charles Lauritsen, ***go!*** s Chief Operating Officer and Joe Bock, ***go!*** s Chief Marketing Officer. The complaint was filed in state court in Hawaii and contains 11 counts and seeks damages and injunctive relief. The clear purpose of the complaint is to blunt Mesa s entry into the Hawaii inter-island market segment. Aloha alleges that Mesa s inter-island air fares are below cost and that Mesa is, therefore, violating specific provisions of Hawaii antitrust and unfair competition law. Aloha also alleges breach of contract and fraud by Mesa in connection with two confidentiality agreements, one in 2005 and the other in 2006.

In 1992, The Supreme Court of the United States decided Morales v. TWA, in which it construed the Airline Deregulation Act as prohibiting any state court, under any state law legal theory, from adjudicating issues which implicated an air carrier s pricing (or other service) practices. Accordingly, an airline s pricing decisions can be attacked only under federal laws. In response to the complaint, Mesa filed a motion on December 8 seeking dismissal of all claims which rest on Mesa s alleged below-cost pricing.

Mesa also denies any improper use of the data furnished by Aloha while Mesa was considering a bid for Aloha during its bankruptcy. The case is in its incipient stages and no trial date has yet been set.

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We are involved in various legal proceedings and FAA civil action proceedings that the Company does not believe will have a material adverse effect upon the Company s business, financial condition or results of operations, although no assurance can be given to the ultimate outcome of any such proceedings.

Item 4. ***Submission of Matters to a Vote of Security Holders***

None.

Executive Officers of the Registrant

The following table sets forth the names and ages of the executive officers of the Company and certain additional information:

Name	Age	Position
Jonathan G. Ornstein	49	Chief Executive Officer
Michael J. Lotz	46	President and Chief Operating Officer
George Murnane III	48	Executive Vice President and Chief Financial Officer
Michael Ferverda	62	Senior Vice President Operations
Brian S. Gillman	37	Senior Vice President, General Counsel and Secretary
David K. Butler	51	Senior Vice President, Administration & Human Resources

Jonathan G. Ornstein was appointed President and Chief Executive Officer of Mesa Air Group, Inc. effective May 1, 1998. Mr. Ornstein relinquished his position as President of the Company in June 2000. From April 1996 to his joining the Company as Chief Executive Officer, Mr. Ornstein served as President and Chief Executive Officer and Chairman of Virgin Express S.A./N.V., a European airline. From 1995 to April 1996, Mr. Ornstein served as Chief Executive Officer of Virgin Express Holdings, Inc. Mr. Ornstein joined Continental Express Airlines, Inc., as President and Chief Executive Officer in July 1994 and, in November 1994, was named Senior Vice President, Airport Services at Continental Airlines, Inc. Mr. Ornstein was previously employed by the Company from 1988 to 1994, as Executive Vice President and as President of the Company s WestAir Holding, Inc. subsidiary.

Michael J. Lotz, President and Chief Operating Officer, joined the Company in July 1998. In January 1999, Mr. Lotz became Chief Operating Officer. In August 1999, Mr. Lotz became the Company s Chief Financial Officer and in January 2000 returned to the position of Chief Operating Officer. On June 22, 2000, Mr. Lotz was appointed President of the Company. Prior to joining the Company, Mr. Lotz served as Chief Operating Officer of Virgin Express, S.A./N.V., a position he held from October 1996 to June 1998. Previously, Mr. Lotz was employed by Continental Airlines, Inc., most recently as Vice President of Airport Operations, Properties and Facilities at Continental Express.

George Murnane III, Executive Vice President and Chief Financial Officer, was appointed Executive Vice President of the Company effective December 2001 and Chief Financial Officer in January 2003. Mr. Murnane served as a director of the Company from June 1999 until October 2003. From 1996 to December 2001, Mr. Murnane was a Director and Executive Vice President of International Airline Support Group, Inc., a re-distributor of aftermarket commercial aircraft spare parts and lessor and trader of commercial aircraft and engines, most recently as its Chief Operating Officer. From 1995 to 1996, Mr. Murnane served as Executive Vice President and Chief Operating Officer of Atlas Air, Inc., an air cargo company. From 1986 to 1996, he was an investment banker with the New York investment banking firm of Merrill Lynch & Co., most recently as a Director in the firm s Transportation Group.

Michael Ferverda, Senior Vice President Operations, joined the Company in 1990. He was appointed President of Freedom Airlines in May 2002 and Senior Vice President Operations in February 2003. Prior to the appointments, Mr. Ferverda served as the Senior Vice President of Operations for Mesa Airlines, Inc. Mr. Ferverda has served the Company in various capacities including pilot, Flight Instructor/Check Airman, Assistant Chief Pilot, FAA Designated Examiner, FAA Director of Operations and Divisional Vice President. Mr. Ferverda was a pilot with Eastern Airlines from 1973 to 1989. Prior to joining Eastern Airlines, Mr. Ferverda served as an Aviator in the United States Navy. Mr. Ferverda is a graduate of Indiana University.

Brian S. Gillman, Senior Vice President, General Counsel and Secretary, joined the Company in February 2001. From July 1996 to February 2001, he served as Vice President, General Counsel and Secretary of Vanguard Airlines, Inc. in Kansas City, Missouri. From September 1994 to July 1996, Mr. Gillman was a corporate associate in the law firm of Stinson, Mag & Fizzell, P.C., Kansas City, Missouri. Mr. Gillman received his Juris Doctorate and B.B.A. in Accounting from the University of Iowa in 1994 and 1991, respectively.

David K. Butler, Senior Vice President, Administration & Human Resources, joined the Company in November 2006. From August 2003 to November 2006, he served as Vice President for Human Resources of Arizona State University in Tempe, Arizona. From May 1999 to August 2003, he served as Vice President for Human Resources for the Durham and Manchester campuses of the University of New Hampshire. Mr. Butler received his Master of Arts in Organizational Management from the University of Phoenix in 1998 and he received his Bachelor of Arts in Human Services from California State University in 1980.

PART II

Item 5. *Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*

Market Price of Common Stock

The following table sets forth, for the periods indicated, the high and low price per share of Mesa common stock for the two most recent fiscal years, as reported by NASDAQ. Mesa s common stock is traded on the NASDAQ Global Market under the symbol MESA.

	Fiscal 2006		Fiscal 2005	
Quarter	**High**	**Low**	**High**	**Low**
First	$ 11.98	$ 8.45	$ 8.03	$ 5.21
Second	12.70	10.47	7.93	6.29
Third	11.14	8.69	7.00	5.25
Fourth	10.18	7.36	8.66	6.76

On December 1, 2006, we had 1,024 shareholders of record. We have never paid cash dividends on our common stock. The payment of future dividends is within the discretion of our board of directors and will depend upon our future earnings, if any, our capital requirements, bank financing, financial condition and other relevant factors.

Recent Sales of Unregistered Securities

On February 7, 2002, in connection with an agreement entered into with Raytheon Aircraft Company (Raytheon), we granted Raytheon a warrant to purchase up to 233,068 shares of our common stock at a per share exercise price of $10. Raytheon must pay a purchase price of $1.50 per share underlying the warrant. The warrant is exercisable at any time over a three-year period following its date of issuance. Absent a default by us under the agreement with Raytheon in which case vesting is accelerated, the shares underlying the warrant vested (and are therefore purchasable by Raytheon) according to the following schedule: 13,401 shares in fiscal year 2001; 116,534 shares in fiscal year 2002; 58,267 shares in fiscal year 2003 and 44,866 shares in fiscal year 2004. As of December 1, 2004, Raytheon has exercised its option to purchase all of the components of the warrant. The sale of the warrant and the shares underlying the warrant were made pursuant to an exemption from registration pursuant to Section 4(2) under the Securities Act of 1933, as amended. In October 2006, a registration statement filed by the Company covering the resale of the shares underlying the warrant was declared effective by the Securities and Exchange Commission.

In June 2003, we completed the private placement of senior convertible notes due 2023, raising approximately $96.9 million net proceeds. The principal underwriter was Merrill Lynch & Co. and the purchasers were qualified

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institutional buyers. At maturity, the principal amount of each note will be $1,000 and the aggregate amount due will be $252 million. These notes are convertible into shares of our common stock at a conversion rate of 39.727 shares per $1,000 in principal amount at maturity of the notes, which equals a conversion price of $10.00 per share. This conversion rate is subject to adjustment in certain circumstances. Holders of these notes may convert their notes only if: (i) the sale price of our common stock exceeds 110% of the accreted conversion price for at least 20 trading days in the 30 consecutive trading days ending on the last trading day of the preceding quarter; (ii) prior to June 16, 2018, the trading price for these notes falls below certain thresholds; (iii) these notes have been called for redemption; or (iv) specified corporate transactions occur. These notes became convertible September 30, 2003. We may redeem these notes, in whole or in part, beginning on June 16, 2008, at a redemption price equal to the issue price, plus accrued original issue discount, plus any accrued and unpaid cash interest. The holders of these notes may require us to repurchase the notes on June 16, 2008 at a price of $397.27 per note plus accrued and unpaid cash interest, if any, on June 16, 2013 at a price of $540.41 per note plus accrued and unpaid cash interest, if any, and on June 16, 2018 at a price of $735.13 per note plus accrued and unpaid cash interest, if any.

In February 2004, we completed the private placement of senior convertible notes due 2024, raising approximately $97.0 million net proceeds. The principal underwriter was Merrill Lynch & Co. and the purchasers were qualified institutional buyers. At maturity, the principal amount of each note will be $1,000 and the aggregate amount due will be $171.4 million. These notes are convertible into shares of our common stock at a conversion rate of 40.3737 shares per $1,000 in principal amount at maturity of the notes, which equals a conversion price of $14.45 per share. This conversion rate is subject to adjustment in certain circumstances. Holders of these notes may convert their notes only if: (i) the sale price of our common stock exceeds 110% of the accreted conversion price for at least 20 trading days in the 30 consecutive trading days ending on the last trading day of the preceding quarter; (ii) prior to February 10, 2019, the trading price for these notes falls below certain thresholds; (iii) these notes have been called for redemption; or (iv) specified corporate transactions occur. These notes are not yet convertible. We may redeem these notes, in whole or in part, beginning on February 10, 2009, at a redemption price equal to the issue price, plus accrued original issue discount, plus any accrued and unpaid cash interest. The holders of the notes may require us to repurchase the notes on February 10, 2009 at a price of $583.4 per note plus accrued and unpaid cash interest, if any, on February 10, 2014 at a price of $698.20 per note plus accrued and unpaid cash interest, if any, and on February 10, 2019 at a price of $835.58 per note plus accrued and unpaid cash interest, if any.

The following table sets forth information required regarding repurchases of common stock that we made during the three months ended September 30, 2006.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan(1)	Maximum Number of Shares That May yet be Purchased Under the Plan
July 2006	75,700	$ 8.50	8,188,367	11,233,894
August 2006	1,768,796	$ 7.77	9,950,863	9,465,098
September 2006	473,377	$ 7.61	10,356,943	8,991,721

(1) Under resolutions adopted and publicly announced in December 1999, January 2001, October 2002, October 2004, April 2005 and October 2005, our Board of Directors has authorized the repurchase, of up to an aggregate of approximately 19.4 million shares of our common stock. Purchases are made at management s discretion based on market conditions and the Company s financial resources. As of September 30, 2006 the Company has spent approximately $66.7 million to purchase and retire approximately 10.4 million shares of its outstanding common stock.

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Item 6. *Selected Financial Data*

Selected Financial Data and Operating Statistics

The selected financial data as of and for each of the five years ended September 30, 2006, are derived from the Consolidated Financial Statements of the Company and its subsidiaries and should be read in conjunction with the Consolidated Financial Statements included elsewhere in this Form 10-K and the related notes thereto and MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Consolidated Statement of Operations and Balance Sheet data in thousands of dollars.

	2006(1)	2005(2)	2004(3)	2003(4)	2002(5)
Consolidated Statement of Operations Data:					
Operating revenues	$ 1,337,197	$ 1,136,268	$ 896,812	$ 599,990	$ 496,783
Operating expenses	1,236,395	1,007,006	829,454	544,711	503,343
Operating income (loss)	100,802	129,262	67,358	55,279	(6,560)
Interest expense	37,305	44,466	25,063	12,664	7,983
Income (loss) before income taxes	56,706	92,166	45,181	41,020	(16,405)
Net income (loss)	33,967	56,867	26,282	25,305	(11,268)
Net income (loss) per share:					
Basic	$ 1.01	$ 1.95	$ 0.83	$ 0.80	$ (0.34)
Diluted	0.84	1.35	0.66	0.76	(0.34)
Consolidated Balance Sheet Data:					
Working capital (deficit)	$ 195,707	$ 236,112	$ 16,046	$ (57,380)	$ 27,483
Total assets	1,238,213	1,167,671	1,121,537	716,936	399,161
Long-term debt, excluding current portion	542,569	636,582	550,613	199,023	110,210
Stockholders equity	264,210	176,670	128,904	111,973	86,758
Consolidated Operating Statistics:					
Passengers carried	14,839,701	13,088,872	10,239,915	6,444,459	5,118,839
Revenue passenger miles (000)	6,840,101	6,185,864	5,035,165	2,814,480	1,986,164
Available seat miles (ASM) (000)	9,139,340	8,715,749	7,107,684	4,453,707	3,459,427
Block hours	571,827	571,339	513,881	393,335	352,323
Average passenger journey in miles	461	473	492	436	388
Average stage length in miles	397	389	390	337	298

Load factor	74.8%	71.0%	70.8%	63.2%	57.4%
Break-even passenger load factor	61.1%	53.3%	53.6%	46.3%	60.1%
Revenue per ASM in cents	14.6	13.0	12.6	13.4	14.4
Operating cost per ASM in cents	13.5	11.6	11.7	12.3	14.6
Average yield per revenue passenger mile in cents	19.5	18.4	17.8	21.3	25.0

	2006(1)	2005(2)	2004(3)	2003(4)	2002(5)
Average fare	$ 87.96	$ 84.25	$ 84.81	$ 89.44	$ 93.93
Aircraft in service	191	182	180	150	124
Cities served	173	176	181	163	147
Number of employees	5,200	4,600	5,000	3,600	3,100

(1) Net income in fiscal 2006 includes a bankruptcy settlement of $12.1 million (pretax) and debt conversion costs of $13.1 million (pretax).

(2) Net income in fiscal 2005 includes the net effect of reversing certain impairment and restructuring charges of $1.3 million (pretax).

(3) Net income in fiscal 2004 includes the net effect of impairment and restructuring charges of $11.9 million (pretax).

(4) Net income in fiscal 2003 includes the effect of impairment and restructuring charges of $1.1 million (pretax) and the reversal of impairment and restructuring charges of $12.0 million (pretax).

(5) Net loss in fiscal 2002 includes the effect of impairment and restructuring charges of $26.7 million (pretax).

Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations*

The following discussion and analysis provides information which management believes is relevant to an assessment and understanding of the Company s results of operations and financial condition. The discussion should be read in conjunction with the Consolidated Financial Statements and the related notes thereto, and the Selected Financial Data and Operating Statistics contained elsewhere in this Form 10-K.

Executive Overview

Fiscal year 2006 was a year of transition for us. As a result of Pre-Merger US Airways emergence from bankruptcy in connection with their merger with America West Airlines and their non-assumption of our code-share agreement, we worked with Pre-Merger US Airways to provide for an orderly transition of aircraft from Pre-Merger US Airways to United and Delta. The transition of aircraft out of Pre-Merger US Airways was completed in the third quarter, and we completed the placement of the last of these aircraft into operations shortly after fiscal year end. As a result of this transition, we were negatively impacted by idle aircraft not earning revenue while in transition as well as incurring significant costs in training pilots while moving aircraft to the Freedom certificate, operations under which perform services for Delta Air Lines.

Fiscal 2006 also saw the launch of ***go!***, Mesa s independent operation in Hawaii. ***go!*** provides inter-island service using five 50-seat CRJ-200 aircraft in a high quality, high frequency service, connecting the islands of Hawaii with service to the Hilo, Honolulu, Kona, Lihue and Maui (Kahului) markets. ***go!*** operates 62 flights per day between Honolulu and Lihue, Kahaluli and Kona.

Also during 2006:

Code-Share Agreements

Freedom commenced operations with Delta in October 2005 and is contracted to operate up to 30 50-seat regional jet aircraft on routes throughout Delta s network. However, Delta has not yet assumed our code-share agreement in its bankruptcy proceedings and could choose to terminate our agreement at any time prior to its emergence from bankruptcy. In March 2006, Freedom expanded its strategic partnership with Delta by signing a three-year agreement to fly up to twelve, 37-seat, De Havilland Dash-8 aircraft in support of Delta s expanding operations at its New York-JFK hub. This Dash-8 agreement was entered into post-petition and does not need to be assumed in the bankruptcy proceedings.

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Fleet

The transition plan described above included moving 36 ERJ-145 and 23 CRJ-200 aircraft out of US Airways and into Delta and United. As of September 30, 2006, we had moved 28 ERJ-145 aircraft into Delta operations and 23 CRJ-200 and eight ERJ-145 aircraft into United operations. We transitioned two ERJ-145 aircraft from United to Delta shortly after our fiscal year end.

Also during fiscal 2006, we added one CRJ-900 to our US Airways fleet, six CRJ-200s (five into our ***go!*** operation and one into our United fleet) and removed two CRJ-200s from our US Airways fleet. In addition, we added six Dash-8 aircraft into our Delta fleet and reduced our Beechcraft 1900D fleet by two by retiring one aircraft and leasing one (the tenth) to Big Sky.

Aircraft in Operation at September 30,

Type of Aircraft	**2006**	**2005**	**2004**
CRJ-200/100 Regional Jet	60	56	54
CRJ-700 Regional Jet	15	15	15
CRJ-900 Regional Jet	38	37	24
Embraer 145 Regional Jet	36	36	36
Beechcraft 1900D	20	22	35
Dash-8	22	16	16
Total	191	182	180

Debt to Equity Conversion

In the first and second quarters of fiscal 2006, holders of $156.8 million in aggregate principal amount at maturity ($62.3 million carrying amount) of the Company s Senior Convertible Notes due 2023 (the Notes) converted their Notes into shares of Mesa common stock. In connection with these conversions, the Company issued an aggregate of 6.2 million shares of Mesa common stock and also paid approximately $11.3 million in debt conversion costs to these Noteholders. The Company also wrote off $1.8 million in debt issue costs related to these notes.

Rotable Spare Parts Maintenance Agreements

In fiscal 2005, we entered into a ten-year agreement with AAR Corp. (the AAR Agreement), for the management and repair of certain of our CRJ-200, -700, -900 and ERJ-145 aircraft rotable spare parts inventory. The agreement was completed in November 2005. Under the AAR agreement, AAR purchased certain of our existing rotable spare parts inventory for $39.5 million in cash and $21.5 million in notes receivable, which we will receive over the next three years.

Summary of Financial Results

Mesa Air Group recorded consolidated net income of $34.0 million in fiscal 2006, representing diluted earnings per share of $0.84. This compares to consolidated net income of $56.9 million or $1.35 per share in fiscal 2005 and consolidated net income of $26.3 million or $0.66 per share in fiscal 2004.

Approximately 98% of our consolidated passenger revenues for the fiscal year ended September 30, 2006 were derived from operations associated with code-share agreements. Our subsidiaries have code-share agreements with US Airways, Delta Air Lines, Midwest Airlines and United Airlines. The remaining passenger revenues are derived from our independent operations, ***go!*** and Mesa Airlines.

Approximately 97% of our passenger revenue was associated with revenue-guarantee code-share agreements. Under the terms of our revenue-guarantee agreements, our major carrier partner controls the marketing, scheduling, ticketing, pricing and seat inventories. Our role is simply to operate our fleet in the safest and most reliable manner in exchange for fees paid under a generally fixed payment schedule. We receive a guaranteed payment based upon a fixed minimum monthly amount plus amounts related to departures and block hours flown in addition to direct

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reimbursement of expenses such as fuel, landing fees and insurance. Among other advantages, revenue-guarantee arrangements reduce our exposure to fluctuations in passenger traffic and fare levels, as well as fuel prices. In fiscal 2006, approximately 96% of our fuel purchases were reimbursed under revenue-guarantee code-share agreements.

Results of Operations

The following tables set forth selected operating and financial data of the Company for the years indicated below.

	Operating Data Years Ended September 30, 2006	2005	2004
Passengers	14,839,701	13,088,872	10,239,915
Available seat miles (ASM)(000s)	9,139,340	8,715,749	7,107,684
Revenue passenger miles (000s)	6,840,101	6,185,864	5,035,165
Load factor	74.8%	71.0%	70.8%
Yield per revenue passenger mile (cents)	19.5	18.4	17.8
Revenue per ASM (cents)	14.6	13.0	12.6
Operating cost per ASM (cents)	13.5	11.6	11.7
Average stage length (miles)	397	389	390
Number of operating aircraft in fleet	191	182	180
Gallons of fuel consumed	211,434,140	202,410,695	170,867,222
Block hours flown	571,827	571,339	513,881
Departures	389,883	391,086	353,083

Operating Expense Data

Years Ended September 30, 2006, 2005 and 2004

	2006			2005			2004		
	Amount (000s)	Percent of Total Revenues	Cost per ASM (cents)	Amount (000s)	Percent of Total Revenues	Cost per ASM (cents)	Amount (000s)	Percent of Total Revenues	Cost per ASM (cents
ght operations	$ 373,283	27.9%	4.1	$ 319,271	28.1%	3.7	$ 297,521	33.2%	4.
el	459,608	34.4%	5.0	304,256	26.8%	3.5	194,510	21.7%	2.
aintenance	233,603	17.5%	2.6	198,695	17.5%	2.3	163,463	18.2%	2.
rcraft & traffic servicing	79,645	6.0%	0.9	68,475	6.0%	0.8	66,223	7.4%	0.
omotion & sales	5,222	0.4%	0.1	3,906	0.3%	0.0	5,806	0.6%	0.
eneral & administrative	60,595	4.5%	0.7	69,429	6.1%	0.8	62,035	6.9%	0.
epreciation & amortization	36,537	2.7%	0.4	44,231	3.9%	0.5	28,001	3.2%	0.
ankruptcy settlement	(12,098)	0.9%	(0.1)						
				(1,257)	(0.1)%	(0.0)	11,895	1.3%	0.

npairment and restructuring arges (credits)									
otal operating expenses	1,236,395	92.5%	13.5	1,007,006	88.6%	11.6	829,454	92.5%	11.7
terest expense	(37,305)	2.8%	(0.4)	(44,466)	3.9%	(0.5)	(25,063)	2.8%	(0.4
terest income	12,116	0.9%	0.1	2,901	0.3%	0.0	1,163	0.1%	0.0
her income (expense)	(16,417)	1.2%	(0.2)	4,469	0.4%	0.1	1,723	0.0%	0.0

Note: Numbers in the table above may not be recalculated due to rounding

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Year Ended September 30, 2006 (000 s)	Mesa/ Freedom	Air Midwest/ *go!*	Other	Elimination	Total
Total operating revenues	$ 1,272,206	$ 61,459	$ 247,474	$ (243,942)	$ 1,337,197
Total operating expenses	1,165,294	71,986	209,381	(210,266)	1,236,395
Operating income (loss)	106,912	(10,527)	38,093	(33,676)	100,802

Year Ended September 30, 2005 (000 s)	Mesa	Air Midwest/ Freedom	Other	Elimination	Total
Total operating revenues	$ 1,064,093	$ 62,681	$ 297,764	$ (288,270)	$ 1,136,268
Total operating expenses	925,783	70,163	255,909	(244,849)	1,007,006
Operating income (loss)	138,310	(7,482)	41,855	(43,421)	129,262

Year Ended September 30, 2004 (000 s)	Mesa/ Freedom	Air Midwest	Other	Elimination	Total
Total operating revenues	$ 807,736	$ 81,714	$ 365,858	$ (358,496)	$ 896,812
Total operating expenses	725,975	91,349	313,243	(301,113)	829,454
Operating income (loss)	81,761	(9,635)	52,615	(57,383)	67,358

All of the Company s 34 Beechcraft 1900D aircraft are owned by Mesa Airlines; however, the Company currently operates 20 of these aircraft. The operating aircraft and debt are recorded on the separate company financial statements of Mesa Airlines, but are operated by Air Midwest, and as a result, Mesa charges Air Midwest rent to offset its depreciation and interest cost. Prior impairment charges related to these aircraft are recorded on the separate company financial statements of Mesa Airlines. The non-operating aircraft are being subleased to other carriers and, as a result, the sublease income, depreciation and interest are included in the other segment.

Fiscal 2006 Versus Fiscal 2005

Operating Revenues

In fiscal 2006, operating revenue increased by $200.9 million, or 17.7%, from $1.1 billion in the twelve months ended September 30, 2005 to $1.3 billion in the twelve months ended September 30, 2006. The increase in revenue is primarily attributable to a $208.1 million increase in operating revenues in the Mesa / Freedom segment, the largest component of which is a $155.8 million increase in fuel reimbursements by our code-share partners. Operating revenues in the Air Midwest / ***go!*** segment decreased $1.2 million, primarily as a result of a $1.9 million decrease in

Essential Air Service (EAS) revenue due to the timing of awards won and lost during the year. In addition, prorate revenue increased $2.9 million in the Air Midwest / ***go!*** segment, primarily from the startup of operations at ***go!*** This net increase was offset by a decrease in Air Midwest prorate revenue as a result of leasing additional Beechcraft 1900D aircraft to other carriers.

Operating Expenses

Flight Operations

In fiscal 2006, flight operations expense increased $54.0 million, or 16.9%, to $373.3 million from $319.3 million for fiscal 2005. On an ASM basis, flight operations expense increased 10.8% to 4.1 cents per ASM in fiscal 2006 from 3.7 cents per ASM in the fiscal 2005. Flight operations expense in the Mesa / Freedom segment increased $59.2 million, which included a $35.2 million increase in aircraft lease cost due to the sale and leaseback of 15 CRJ-900 aircraft in September 2005, a $12.7 million increase in flight crew wages, a $4.0 million increase in lodging cost and a $2.6 million increase in flight simulator lease expense. The increases in flight crew wages, lodging cost and flight simulator expenses are a result of training costs associated with the transition of aircraft onto the Freedom certificate as well as the start up of the Company s Delta Dash-8 operations at New York s JFK airport. Flight operations expense in the Air Midwest / ***go!*** segment increased $2.0 million primarily as a result of the startup of operations at ***go!***

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Fuel

In fiscal 2006, fuel expense increased $155.3 million, or 51.1%, to $459.6 million from $304.3 million for fiscal 2005. On an ASM basis, fuel expense increased 42.9% to 5.0 cents per ASM in fiscal 2006 from 3.5 cents per ASM in fiscal 2005. Into-plane fuel cost in fiscal 2006 increased 44.7% from $1.50 per gallon in fiscal 2005 to $2.17 per gallon in fiscal 2006, resulting in a $136.1 million unfavorable price variance. Consumption increased 4% in fiscal 2006 resulting in a $19.2 million unfavorable volume variance. In fiscal 2006, approximately 96% of our fuel costs were reimbursed by our code-share partners.

Maintenance Expense

In fiscal 2006, maintenance expense increased $34.9 million, or 17.6%, to $233.6 million from $198.7 million for fiscal 2005. On an ASM basis, maintenance expense increased 13.0% to 2.6 cents per ASM in fiscal 2006 from 2.3 cents per ASM in fiscal 2005. Maintenance expense in the Mesa / Freedom segment increased $46.1 million, which included an $11.1 million increase in aircraft heavy maintenance expense, an $11.2 million increase in rotable spare part repair and rent expense, a $7.8 million increase in engine maintenance, a $5.0 million increase in materials, repairs and servicing expenses, a $3.6 million increase in mechanic wage expenses, and a $2.3 million increase in hangar rent. The increase is due to the timing of certain maintenance events for the Company s aircraft and the additional bases established to support the United and Delta operations. Maintenance expense in the Air Midwest / ***go***! segment decreased $2.6 million. The net decrease was due to a $4.5 million reduction in maintenance expense primarily due to the costs associated with preparing Beechcraft 1900 aircraft for lease to other carriers in fiscal 2005, this decrease was offset by a $1.9 million increase as a result of the start up of ***go!***

Aircraft and Traffic Servicing

In fiscal 2006, aircraft and traffic servicing expense increased by $11.2 million, or 16.3%, to $79.6 million from $68.5 million for fiscal 2005. On an ASM basis, aircraft and traffic servicing expense increased 12.5% to 0.9 cents per ASM in fiscal 2006 from 0.8 cents per ASM in fiscal 2005. Aircraft and traffic servicing expense in the Mesa / Freedom segment increased $10.7 million, which included a $5.6 million increase in station rents and a $4.5 million increase in passenger related costs, primarily landing fees. These increases were primarily a result of moving into higher cost East Coast cities for United and Delta. These costs are reimbursed by our code-share partners. Aircraft and traffic servicing expense in the Air Midwest / ***go!*** segment remained relatively constant with decreases at Air Midwest due to reduced capacity being offset by increases at ***go!*** as a result of the startup.

Promotion and Sales

In fiscal 2006, promotion and sales expense increased by $1.3 million, or 33.7%, to $5.2 million from $3.9 million for fiscal 2005. On an ASM basis, promotion and sales expense increased 100% to 0.1 cents per ASM in the twelve months ended September 30, 2006 from 0.0 cents per ASM in the twelve months ended September 30, 2005. Promotion and sales expense in the Air Midwest / ***go!*** segment increased $1.3 million, with increases at ***go!*** due to the startup being offset by decreases at Air Midwest as a result of reduced capacity. We do not pay promotion and sales expenses under our regional jet revenue-guarantee contracts.

General and Administrative

In fiscal 2006, general and administrative expense decreased $8.8 million, or 12.7%, to $60.6 million from $69.4 million for fiscal 2005. On an ASM basis, general and administrative expense decreased 12.5% to 0.7 cents per ASM in fiscal 2006 from 0.8 cents per ASM in fiscal 2005. The net decrease included a $13.5 million reduction in bad debt expense due to the reversal of reserves for $7.2 million as a result of proceeds received from the Pre-Merger US

Airways bankruptcy settlement and other items which were established in fiscal 2005, a $4.0 million reduction in medical expenses due to a change in health plans, a $1.0 million reduction in passenger liability insurance premiums as a result of lower rates and a $2.1 million reduction in bonus wages as a result of a failure to meet profitability targets. These decreases were offset by a $2.3 million increase in stock option expense due to the adoptions of SFAS 123(R), which requires expensing stock options; a $1.9 million increase in legal costs due to the litigation involving our commencement of service in the Hawaii inter-island market in fiscal 2006 and a $0.8 million favorable settlement in fiscal 2005; and a $1.7 million increase in workers compensation expense due to an increase in claims.

Depreciation and Amortization

In fiscal 2006, depreciation and amortization expense decreased $7.7 million, or 17.4%, to $36.5 million from $44.2 million for fiscal 2005. On an ASM basis, depreciation expense decreased 20% to 0.4 cents per ASM in fiscal 2006 from 0.5 cents per ASM in fiscal 2005. The decrease was primarily due to a $7.2 million reduction in depreciation expense in the Mesa / Freedom segment as a result of permanently financing 15 CRJ-900 aircraft as operating leases in the fourth quarter of fiscal 2005.

Bankruptcy Settlement

In fiscal 2006, the Company received approximately 350,000 shares of US Airways common stock as part of our bankruptcy claim against Pre-Merger US Airways. The shares were valued at approximately $50 per share, hence the Company recognized approximately $17.6 million in benefit from its claim. Of the $17.6 million, $5.5 million was applied to receivables that were previously reserved.

Impairment and Restructuring Charges

In fiscal 2005, we reversed $1.3 million in reserves for lease and lease return costs related to two Shorts 360 aircraft the Company returned to the lessor in January 2005.

Interest Expense

In fiscal 2006, interest expense decreased $7.2 million, or 16.1%, to $37.3 million from $44.5 million for fiscal 2005. On an ASM basis, interest expense decreased 20% to 0.4 cents per ASM in fiscal 2006 from 0.5 cents per ASM in fiscal 2005. The net decrease in interest expense was primarily due a $10.4 million reduction in interest expense as a result of permanently financing 15 CRJ-900 aircraft with operating leases in the fourth quarter of fiscal 2005, a $2.8 million reduction in convertible debt interest expense as a result of the conversion from debt to equity and a $1.0 million reduction in interest expense related to the financing of rotable inventory that was retired in the first quarter of fiscal 2006. These decreases were partially offset by a $6.4 million increase in interest expense on aircraft financing as a result of increases in variable interest rates.

Interest Income

In fiscal 2006, interest income increased $9.2 million to $12.1 million from $2.9 million for fiscal 2005. The increase is due to increases in the rates of return on our portfolio of marketable securities.

Other Income (Expense)

In fiscal 2006, other income (expense) decreased $20.9 million from income of $4.5 million for fiscal 2005 to expense of $16.4 million for fiscal 2006. In fiscal 2006, other income (expense) is primarily comprised of $13.1 million in debt conversion costs and $2.5 million in losses on investment securities.

In fiscal 2005, other income was primarily comprised of net investment income of $2.3 million from the Company s portfolio of investment securities, $2.9 million of dividend income on marketable securities, $1.0 million income from a settlement of a dispute with a vendor and $1.7 million in net costs to return four non-operating EMB120 aircraft to the lessor.

Income Taxes

In fiscal 2006, the our effective tax rate increased from 38.3% for fiscal 2005 to 40.1%. The increase in our effective tax rate is mainly due to the inability to deduct stock option expense related to incentive stock options for income tax purposes.

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Fiscal 2005 Versus Fiscal 2004

Operating Revenues

In fiscal 2005, operating revenue increased by $239.5 million, or 26.7%, from $896.8 million to $1,136.3 million. The increase in revenue is primarily attributable to a $256.9 million increase in revenue associated with the operation of 15 additional regional jets flown by Mesa compared to 2004. Offsetting this increase was a decrease in passenger revenue of approximately $20.3 million in the Air Midwest / Freedom segment. The decrease in passenger revenue in the Air Midwest / Freedom segment primarily due to reductions in capacity as the Company has leased nine Beechcraft 1900 aircraft to Big Sky and four Beechcraft 1900 aircraft to Great Lakes during fiscal 2005. However, EAS subsidies received by Air Midwest increased by $1.3 million as a result of additional markets served and higher subsidy rates on existing markets.

Operating Expenses

Flight Operations

In fiscal 2005, flight operations expense increased $21.8 million or 7.3%, to $319.3 million from $297.5 million for fiscal 2004. On an ASM basis, flight operations expense decreased 11.9% to 3.7 cents per ASM in fiscal 2005 from 4.2 cents per ASM in fiscal 2004. This increase in total expense is primarily attributed to a $15.8 million increase in aircraft lease costs as a result of placing additional regional jets into service and an increase of $5.0 million in pilot and flight attendant wages due to growth in flight operations. The decrease on an ASM basis is due to the addition of larger regional jets at Mesa and the reduction in turboprop aircraft flown by Air Midwest.

Fuel

In fiscal 2005, fuel expense increased $109.7 million or 56.4%, to $304.3 million from $194.5 million for fiscal 2004. On an ASM basis, fuel expense increased 29.6% to 3.5 cents per ASM in fiscal 2005 from 2.7 cents per ASM in fiscal 2004. Into-plane fuel cost increased 32% per gallon, resulting in a $62.3 million unfavorable price variance and consumption increased 18% resulting in a $47.4 million unfavorable volume variance. The increase in volume was due to the additional regional jets added to the fleet. In fiscal 2005, approximately 95% of our fuel costs were reimbursed by our code-share partners.

Maintenance Expense

In fiscal 2005, maintenance expense increased $35.2 million or 21.6%, to $198.7 million from $163.5 million for fiscal 2004. On an ASM basis, maintenance expense remained flat at 2.3 cents for fiscal 2005 and fiscal 2004. The increase is due to $5.5 million in additional aircraft heavy maintenance expense, a $6.6 million increase in component and rent expense, a $10.1 million increase in engine maintenance, and a $13.5 million increase in materials, repairs and servicing expenses. The increase is due to the increased fleet size and age of the Company s aircraft.

Aircraft and Traffic Servicing

In fiscal 2005, aircraft and traffic servicing expense increased by $2.3 million or 3.4%, to $68.5 million from $66.2 million for fiscal 2004. On an ASM basis, aircraft and traffic servicing expense decreased 11.1% to 0.8 cents per ASM in fiscal 2005 from 0.9 cents per ASM in fiscal 2004. The increase in expense is primarily related to an 11% increase in departures. The decrease on an ASM basis is due to the addition of larger regional jets at Mesa and the reduction in turboprop aircraft at Air Midwest.

Promotion and Sales

In fiscal 2005, promotion and sales expense decreased $1.9 million or 32.7%, to $3.9 million from $5.8 million for fiscal 2004. On an ASM basis, promotion and sales expense decreased 100% to 0.0 cents per ASM in fiscal 2005 from 0.1 cents per ASM in fiscal 2004. The decrease in expense is due to a decline in booking and franchise fees paid by Air Midwest under our pro-rate agreements with our code-share partners, caused by a decline in passengers carried under these agreements. We do not pay these fees under our regional jet revenue-guarantee contracts.

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General and Administrative

In fiscal 2005, general and administrative expense increased $7.4 million or 11.9%, to $69.4 million from $62.0 million for fiscal 2004. On an ASM basis, general and administrative expense decreased 11.1% to 0.8 cents per ASM in fiscal 2005 from 0.9 cents per ASM in fiscal 2004. The increase in expense includes a $6.3 million increase in property taxes associated with increases in our fleet and a $2.6 million increase in bad debt expense as a result of increasing the Company s allowance for doubtful receivables related to code-share partners in bankruptcy. Offsetting these increases was a $1.6 million decrease in health insurance costs related to the timing and severity of claims.

Depreciation and Amortization

In fiscal 2005, depreciation and amortization expense increased $16.2 million or 58.0%, to $44.2 million from $28.0 million for fiscal 2004. On an ASM basis, depreciation and amortization expense increased 25.0% to 0.5 cents per ASM in fiscal 2005 from 0.4 cents per ASM in fiscal 2004. The increase in expense is primarily due to the purchase of 13 regional jets in 2005.

Impairment and Restructuring Charges

In fiscal 2005, we reversed $1.3 million in reserves for lease and lease return costs related to two Shorts 360 aircraft the Company returned to the lessor in January 2005.

In fiscal 2004, we recognized an impairment charge of $12.4 million related to the early termination of leases on seven Beechcraft 1900D aircraft. We negotiated the terms of the early return with the majority of the aircraft lessors and took a charge that included $2.4 million for the present value of future lease payments, $2.4 million for the negotiated settlement of return conditions, $1.2 million for the cancellation of maintenance agreements, $0.8 million to reduce maintenance deposits to net realizable value and $4.5 million to reduce the value of rotable and expendable inventory to fair value less costs to sell. We purchased two of the aircraft from the lessors, which were subsequently scrapped. As a result, we also took a $1.1 million impairment charge for the difference between the buy out of the lease and the subsequent sale of the aircraft. These charges were offset by the reversal of $0.5 million of prior year restructuring charges.

Interest Expense

In fiscal 2005, interest expense increased $19.4 million or 77.4%, to $44.5 million from $25.1 million for fiscal 2004. The increase in interest expense is primarily comprised of an increase of $14.6 million on interim and permanently financed aircraft debt, $1.2 million on the senior convertible notes that were issued in February 2004, $1.2 million on the inventory financing arrangement with GECAS and $1.1 million on the Beechcraft 1900 aircraft debt.

Other Income (Expense)

In fiscal 2005, other income increased $2.7 million, or 159.4%, to $4.5 million from $1.7 million for fiscal 2004. In fiscal 2005, other income is primarily comprised of net investment income of $2.3 million from the Company s portfolio of investment securities, $2.9 million of dividend income on marketable securities, $1.0 million income from a settlement of a dispute with a vendor and $1.7 million in net costs to return four non-operating EMB120 aircraft to the lessor.

In fiscal 2004, other income was primarily comprised of investment income of $0.6 million related to the Company s portfolio of investment securities.

Income Taxes

In fiscal 2005, the Company s effective income tax rate was 38.3% as compared to 41.8% in fiscal 2004. The decrease in rate from fiscal 2004 is due to certain payments to top executives in the prior year, a portion of which were not deductible for income taxes.

Liquidity and Capital Resources

Sources and Uses of Cash

At September 30, 2006, we had cash, cash equivalents, and marketable securities (including restricted cash and held-to-maturity securities) of $234.3 million, compared to $280.4 million at September 30, 2005. In fiscal 2006, we cancelled our rotable financing arrangement with GECAS and were required to repay the $19.7 million liability that remained outstanding. The liability was retired with cash of $15.9 million and included offsetting $3.8 million in notes receivable from GECAS. We then entered into a similar arrangement with AAR whereby AAR was required to purchase certain rotable spare parts for $39.6 million in cash and $21.5 million in notes receivable.

Also in fiscal 2006, holders of $156.8 million in aggregate principal amount at maturity ($62.3 million carrying amount) of the Company s Senior Convertible Notes due 2023 (the Notes) converted their Notes into shares of Mesa common stock. In connection with these conversions, the Company paid approximately $11.3 million in debt conversion costs to these Noteholders.

Other uses of cash included capital expenditures of $42.6 million, which was primarily attributable to preparing aircraft for service and provisioning of rotable inventory to support additional bases of operations, and the purchase of $18.6 million of the Company s outstanding common stock.

Our cash and cash equivalents and marketable securities are intended to be used for working capital, capital expenditures, acquisitions, and to fund our obligations with respect to regional jet deliveries.

As of September 30, 2006, we had receivables of approximately $47.4 million (net of an allowance for doubtful accounts of $1.6 million), compared to receivables of approximately $29.0 million (net of an allowance for doubtful accounts of $8.9 million) as of September 30, 2005. The amounts include receivables due from our code-share partners, credits due from the aircraft manufacturer and passenger ticket receivables due through the Airline Clearing House. Accounts receivable from our code-share partners was 45% of total gross accounts receivable at September 30, 2006.

Code-Share Partner in Bankruptcy

On September 14, 2005, Delta Air Lines, Inc. filed for reorganization under Chapter 11 of the US Bankruptcy Code. Delta has not yet assumed our code-share agreement in its bankruptcy proceeding and could choose to seek to renegotiate the agreement on terms less favorable to us or terminate this agreement. As of the date of this report, the Company believes that there is a reasonable likelihood that Delta will assume our code-share agreement in such proceedings. This belief is based primarily on the continued expansion of the aircraft we fly under our agreement with Delta and our current business relations with them. Notwithstanding this belief, no assurance can be given that Delta will assume our code-share agreement or otherwise seek to renegotiate the terms of the agreement. If Delta and the Company did renegotiate the terms of the existing agreement, the Company s profitability would be impacted and liquidity would be reduced. However, if Delta was to terminate our agreement, the Company would seek to mitigate the effect of such event by seeking alternative code-share partners, subleasing the aircraft to another carrier or carriers or parking the aircraft. These options could have a material adverse effect on our liquidity, financial condition and results of operations.

Operating Leases

We have significant long-term lease obligations primarily relating to our aircraft fleet. The leases are classified as operating leases and are therefore excluded from our consolidated balance sheets. At September 30, 2006, we leased

158 aircraft with remaining lease terms ranging from 1 to 17.5 years. Future minimum lease payments due under all long-term operating leases were approximately $2.3 billion at September 30, 2006.

3.625% Senior Convertible Notes due 2024

In February 2004, we completed the private placement of senior convertible notes due 2024, which resulted in gross proceeds of $100.0 million ($97.0 million net). Cash interest is payable on the notes at the rate of 2.115% per year on the aggregate amount due at maturity, payable semiannually in arrears on February 10 and August 10 of

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each year, beginning August 10, 2004, until February 10, 2009. After that date, we will not pay cash interest on the notes prior to maturity, and the notes will begin accruing original issue discount at a rate of 3.625% until maturity. On February 10, 2024, the maturity date of the notes, the principal amount of each note will be $1,000. The aggregate amount due at maturity, including interest accrued from February 10, 2009, will be $171.4 million. Each of our wholly owned domestic subsidiaries guarantees the notes on an unsecured senior basis. The notes and the note guarantees are senior unsecured obligations and rank equally with our existing and future senior unsecured indebtedness. The notes and the note guarantees are junior to the secured obligations of our wholly owned subsidiaries to the extent of the collateral pledged.

The notes were sold at an issue price of $583.40 per note and are convertible into shares of our common stock at a conversion rate of 40.3737 shares per note, which equals a conversion price of $14.45 per share. This conversion rate is subject to adjustment in certain circumstances. Holders of the notes may convert their notes only if: (i) after March 31, 2004, the sale price of our common stock exceeds 110% of the accreted conversion price for at least 20 trading days in the 30 consecutive trading days ending on the last trading day of the preceding quarter; (ii) on or prior to February 10, 2019, the trading price for the notes falls below certain thresholds; (iii) the notes have been called for redemption; or (iv) specified corporate transactions occur. These notes are not yet convertible. We may redeem the notes, in whole or in part, beginning on February 10, 2009, at a redemption price equal to the issue price, plus accrued original issue discount, plus any accrued and unpaid cash interest. The holders of the notes may require us to repurchase the notes on February 10, 2009 at a price of $583.40 per note plus accrued and unpaid cash interest, if any, on February 10, 2014 at a price of $698.20 per note plus accrued and unpaid cash interest, if any, and on February 10, 2019 at a price of $835.58 per note plus accrued and unpaid cash interest, if any.

6.25% Senior Convertible Notes Due 2023

In June 2003, we completed the private placement of senior convertible notes due 2023, which resulted in gross proceeds of $100.1 million ($96.9 million net). Cash interest is payable on the notes at the rate of 2.4829% per year on the aggregate amount due at maturity, payable semiannually in arrears on June 16 and December 16 of each year, beginning December 16, 2003, until June 16, 2008. After that date, we will not pay cash interest on the notes prior to maturity, and the notes will begin accruing original issue discount at a rate of 6.25% until maturity. On June 16, 2023, the maturity date of the notes, the principal amount of each note will be $1,000. The aggregate amount due at maturity, including interest accrued from June 16, 2008, will be $252 million. Each of our wholly owned domestic subsidiaries guarantees the notes on an unsecured senior basis. The notes and the note guarantees are senior unsecured obligations and rank equally with our existing and future senior unsecured indebtedness. The notes and the note guarantees are junior to the secured obligations of our wholly owned subsidiaries to the extent of the collateral pledged.

The notes were sold at an issue price of $397.27 per note and are convertible into shares of our common stock at a conversion rate of 39.727 shares per note, which equals a conversion price of $10 per share. This conversion rate is subject to adjustment in certain circumstances. Holders of the notes may convert their notes only if: (i) the sale price of our common stock exceeds 110% of the accreted conversion price for at least 20 trading days in the 30 consecutive trading days ending on the last trading day of the preceding quarter; (ii) prior to June 16, 2018, the trading price for the notes falls below certain thresholds; (iii) the notes have been called for redemption; or (iv) specified corporate transactions occur. These notes became convertible in 2003. The Company may redeem the notes, in whole or in part, beginning on June 16, 2008, at a redemption price equal to the issue price, plus accrued original issue discount, plus any accrued and unpaid cash interest. The holders of the notes may require the Company to repurchase the notes on June 16, 2008 at a price of $397.27 per note plus accrued and unpaid cash interest, if any, on June 16, 2013 at a price of $540.41 per note plus accrued and unpaid cash interest, if any, and on June 16, 2018 at a price of $735.13 per note plus accrued and unpaid cash interest, if any.

In fiscal 2006, holders of $156.8 million in aggregate principal amount at maturity ($62.3 million carrying amount) of the Company s Senior Convertible Notes due 2023 (the Notes) converted their Notes into shares of Mesa common stock. In connection with these conversions, the Company issued an aggregate of 6.2 million shares of Mesa common stock and also paid approximately $11.3 million in debt conversion costs to these Noteholders. The Company also wrote off $1.8 million in debt issue costs related to these notes.

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Interim and Permanent Aircraft Financing Arrangements

At September 30, 2006, we had an aggregate of $123.1 million in notes payable to an aircraft manufacturer for delivered aircraft on interim financing. Under interim financing arrangements, we take delivery and title of the aircraft prior to securing permanent financing and the acquisition of the aircraft is accounted for as a purchase with debt financing. Accordingly, we reflect the aircraft and debt under interim financing on our balance sheet during the interim financing period. After taking delivery of the aircraft, it is our practice and our intention to subsequently enter into a sale and leaseback transaction with an independent third-party lessor. Upon permanent financing, the proceeds from the sale and leaseback transaction are used to retire the notes payable to the manufacturer. Any gain recognized on the sale and leaseback transaction is deferred and amortized over the life of the lease. At September 30, 2006, we had five aircraft on interim financing with the manufacturer. These interim financings agreements typically have a term of six months and provide for monthly interest only payments at LIBOR plus three percent. The current interim financing agreement with the manufacturer provides for us to have a maximum of 15 aircraft on interim financing at any one time.

Other Indebtedness and Obligations

In October 2004, the Company permanently financed five CRJ-900 aircraft with $118.0 million in debt. The debt bears interest at the monthly LIBOR plus three percent and requires monthly principal and interest payments.

In January and March 2004, the Company permanently financed five CRJ-700 and six CRJ-900 aircraft with $254.7 million in debt. The debt bears interest at the monthly LIBOR plus three percent and requires monthly principal and interest payments.

In December 2003, we assumed $24.1 million of debt in connection with our purchase of two CRJ-200 aircraft in the Midway Chapter 7 bankruptcy proceedings. The debt, due in 2013, bears interest at the rate of 7% per annum through 2008, converting to 12.5% thereafter, with principal and interest due monthly.

As of September 30, 2006, we had $12.0 million in restricted cash on deposit collateralizing various letters of credit outstanding and the ACH funding of our payroll.

Contractual Obligations

As of September 30, 2006, we had $572.2 million of long-term debt (including current maturities). This amount consisted of $431.6 million in notes payable related to owned aircraft, $137.8 in aggregate principal amount of our senior convertible notes due 2023 and 2024 and $2.8 million in other miscellaneous debt.

The following table sets forth our cash obligations (including principal and interest) as of September 30, 2006.

			Payment Due by Period				
Obligations	**2007**	**2008**	**2009**	**2010 (In thousands)**	**2011**	**Thereafter**	**Total**
Long-term debt:							
Note payable related to CRJ700s and 900s(2)	$ 46,896	$ 46,116	$ 45,234	$ 44,346	$ 43,419	$ 297,645	$ 523,656

2003 senior convertible debt notes (assuming no conversions)	2,365	2,365				95,234	99,964
2004 senior convertible debt notes (assuming no conversions)	3,625	3,625	1,813			171,409	180,472
Notes payable related to B1900Ds	11,947	11,939	11,940	28,982	25,156	9,049	99,013
Note payable related to CRJ200s(2)	3,000	3,000	3,000	3,000	3,000	14,952	29,952
Note payable to manufacturer	1,823						1,823
Mortgage note payable	109	109	824				1,042
Other	25	25	25	25	25	25	150
Total long-term debt	69,790	67,179	62,836	76,353	71,600	588,314	936,072