

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

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 1996

OR

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

FOR THE TRANSITION PERIOD FROM _____ TO _____

Commission File Number 0-9781

CONTINENTAL AIRLINES, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

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

2929 Allen Parkway, Suite 2010
Houston, Texas 77019
(Address of principal executive offices)
(Zip Code)

713-834-2950
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

As of October 11, 1996, 9,280,000 shares of Class A common stock and 46,771,324 shares of Class B common stock were outstanding.

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CONTINENTAL AIRLINES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions of dollars, except per share data)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	1996	1995	1996	1995
	(Unaudited)		(Unaudited)	

Operating Revenue:				
Passenger	\$1,546	\$1,402	\$4,440	\$3,997
Cargo, mail and other .	125	113	359	405

	1,671	1,515	4,799	4,402
Operating Expenses:				
Wages, salaries and related costs	397	356	1,139	1,079
Aircraft fuel	201	171	558	508
Commissions	135	126	398	376
Aircraft rentals	128	122	379	370
Maintenance, materials and repairs	118	119	349	317
Other rentals and landing fees	89	87	258	271
Depreciation and amortization	63	63	195	192
Nonrecurring charge	128	-	128	-
Other	335	318	969	998
	1,594	1,362	4,373	4,111
Operating Income	77	153	426	291
Nonoperating Income (Expense):				
Interest expense	(40)	(52)	(129)	(162)
Interest capitalized	1	1	2	5
Interest income	11	9	30	22
Other, net	(2)	2	19	110
	(30)	(40)	(78)	(25)
Income before Income Taxes, Minority Interest and Extraordinary Loss	47	113	348	266
Income Tax Provision	(18)	-	(57)	(78)

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CONTINENTAL AIRLINES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions of dollars, except per share data)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	1996	1995	1996	1995
	(Unaudited)		(Unaudited)	
Income before Minority Interest and Extraordinary Loss	\$ 29	\$ 113	\$ 291	\$ 188
Minority Interest	(1)	(2)	(3)	(5)
Distributions on Preferred Securities of Trust, net of applicable income taxes of \$2 and \$7, respectively	(4)	-	(10)	-
Income before Extraordinary Loss	24	111	278	183
Extraordinary Loss, net of applicable income taxes of \$4	(6)	-	(6)	-
Net Income	18	111	272	183
Preferred Dividend Requirements and Accretion to				

Liquidation Value	(1)	(5)	(3)	(8)
Income Applicable to Common Shares	\$ 17	\$ 106	\$ 269	\$ 175
Earnings per Common and Common Equivalent Share:				
Income Before				
Extraordinary Loss.	\$0.35	\$1.54	\$4.26	\$2.93
Extraordinary Loss, net of tax.	(0.10)	-	(0.10)	-
Net Income	\$0.25	\$1.54	\$4.16	\$2.93

Earnings per Common Share Assuming Full Dilution:				
Income Before				
Extraordinary Loss.	\$0.34	\$1.34	\$3.58	\$2.68
Extraordinary Loss, net of tax.	(0.09)	-	(0.08)	-
Net Income	\$0.25	\$1.34	\$3.50	\$2.68

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

CONTINENTAL AIRLINES, INC.
CONSOLIDATED BALANCE SHEETS
(In millions of dollars, except for share data)

ASSETS	September 30, 1996	December 31, 1995
	(Unaudited)	
Current Assets:		
Cash and cash equivalents, including restricted cash and cash equivalents of \$70 and \$144, respectively.	\$ 865	\$ 747
Accounts receivable, net.	443	351
Spare parts and supplies, net	114	127
Prepayments and other	81	90
Total current assets	1,503	1,315
Property and Equipment:		
Owned property and equipment:		
Flight equipment	1,140	1,107
Other.	317	288
	1,457	1,395
Less: Accumulated depreciation.	353	285
	1,104	1,110
Purchase deposits for flight equipment.	121	48
Capital leases:		
Flight equipment	406	394
Other.	29	28
	435	422
Less: Accumulated amortization	150	119
	285	303
Total property and equipment	1,510	1,461
Other Assets:		
Routes, gates and slots, net.	1,488	1,531
Reorganization value in excess of amounts allocable to identifiable assets, net.	240	251
Investments	131	163
Other assets, net	111	100
Total other assets	1,970	2,045
Total Assets.	\$4,983	\$4,821

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CONTINENTAL AIRLINES, INC.
CONSOLIDATED BALANCE SHEETS
(In millions of dollars, except for share data)

LIABILITIES AND STOCKHOLDERS' EQUITY	September 30, 1996 (Unaudited)	December 31, 1995
Current Liabilities:		
Current maturities of long-term debt.	\$ 205	\$ 163
Current maturities of capital leases.	62	58
Accounts payable.	627	617
Air traffic liability	765	579
Accrued payroll and pensions.	159	181
Accrued other liabilities	311	386
Total current liabilities.	2,129	1,984
Long-Term Debt	1,116	1,352
Capital Leases	275	306
Deferred Credits and Other Long-Term Liabilities:		
Deferred income taxes	84	46
Deferred credit - aircraft operating leases	78	97
Accruals for aircraft retirements and excess facilities.	187	175
Other	244	246
Total deferred credits and other long-term liabilities	593	564
Commitments and Contingencies		
Minority Interest.	16	27
Continental-Obligated Mandatorily Redeemable Preferred Securities of Subsidiary Trust Holding Solely Convertible Subordinated Debentures (A)	242	242
Redeemable Warrants.	50	-
Redeemable Preferred Stock (aggregate redemption value - \$45 and \$41, respectively)	45	41

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CONTINENTAL AIRLINES, INC.
CONSOLIDATED BALANCE SHEETS
(In millions of dollars, except for share data)

September 30, December 31,
1996 1995
(Unaudited)

Common Stockholders' Equity:		
Class A common stock - \$.01 par, 50,000,000 shares authorized; 9,280,000 and 12,602,112 shares issued and outstanding, respectively	\$ -	\$ -
Class B common stock - \$.01 par, 200,000,000 shares authorized; 46,771,324 and 42,856,548 shares issued and outstanding, respectively . .	-	-
Additional paid-in capital	686	733
Accumulated deficit	(156)	(428)
Unvested portion of restricted stock. . .	(6)	(10)
Additional minimum pension liability. . .	(8)	(8)
Unrealized gain on marketable equity securities.	1	18
Total common stockholders' equity. . . .	517	305
Total Liabilities and Stockholders' Equity	\$4,983	\$4,821

(A) The sole assets of the Trust are convertible subordinated debentures with an aggregate principal amount of \$250 million, which bear interest at the rate of 8-1/2% per annum and mature on December 1, 2020. Upon repayment, the Continental-Obligated Mandatorily Redeemable Preferred Securities of Subsidiary Trust will be mandatorily redeemed.

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

CONTINENTAL AIRLINES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions of dollars)

	Nine Months Ended September 30,	
	1996	1995
	(Unaudited)	
Net Cash Provided by Operating Activities.	\$611	\$281
Cash Flows from Investing Activities:		
Proceeds from sale of America West stock and warrants	32	-
Proceeds from disposition of property, equipment and other assets	6	13
Proceeds from sale/leaseback transaction.	12	-
Capital expenditures, net of returned purchase deposits.	(195)	(63)
Purchase deposits refunded in connection with aircraft delivered . .	12	97

Proceeds from System One transactions	-	40
Net cash provided (used) by investing activities.	(133)	87
Cash Flows from Financing Activities:		
Proceeds from issuance of long-term debt, net.	553	8
Payments on long-term debt and capital lease obligations.	(890)	(166)
Proceeds from issuance of common stock.	7	11
Dividends paid on preferred securities of trust	(17)	-
Dividend paid to minority interest holder in connection with secured term loan financing.	(13)	-
Purchase of warrants.	-	(14)
Net cash used by financing activities.	(360)	(161)
Net Increase in Cash and Cash Equivalents.	118	207
Cash and Cash Equivalents - Beginning of Period	747	396
Cash and Cash Equivalents - End of Period.	\$865	\$603

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CONTINENTAL AIRLINES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions of dollars)

	Nine Months Ended September 30,	
	1996	1995
	(Unaudited)	
Supplemental Cash Flow Information:		
Interest paid	\$120	\$136
Income taxes paid	\$ 1	\$ 9
Investing and Financing Activities		
Not Affecting Cash:		
Property and equipment acquired through the issuance of debt	\$ 54	\$ 21
Reclassification of accrued rent, capital leases and interest to long-term debt	\$ 11	\$ 42
Capital lease obligations incurred.	\$ 27	\$ 9
Financed purchase deposits for flight equipment	\$ 17	\$ 5
Return of financed purchase deposits.	\$ -	\$ 10
Reclassification of accrued management fees to long-term debt.	\$ -	\$ 21
Investment in AMADEUS	\$ -	\$120
Reduction of debt in connection with System One transactions.	\$ -	\$ 42
Issuance of debt in connection with purchase of Air Canada warrants.	\$ -	\$ 42
Issuance of convertible secured debentures in connection with the aircraft settlements	\$ -	\$158
Conversion of preferred stock into long-term debt	\$ -	\$ 21

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

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

In the opinion of management, the unaudited consolidated financial statements included herein contain all adjustments necessary to present fairly the financial position, results of operations and cash flows for the periods indicated. Such adjustments are of a normal, recurring nature. The accompanying consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto contained in the Annual Report of Continental Airlines, Inc. (the "Company" or "Continental") on Form 10-K, as amended, for the year ended December 31, 1995.

NOTE 1 - STOCK SPLIT

On June 26, 1996, the Board of Directors of the Company declared a two-for-one stock split (the "Stock Split") pursuant to which (a) one share of the Company's Class A common stock, par value \$.01 per share ("Class A common stock"), was issued for each share of Class A common stock outstanding on July 2, 1996 (the "Record Date") and (b) one share of the Company's Class B common stock, par value \$.01 per share ("Class B common stock"), was issued for each share of Class B common stock outstanding on the Record Date. Shares issuable pursuant to the Stock Split were distributed on or about July 16, 1996. All share and earnings per share information for prior periods has been adjusted for the Stock Split.

NOTE 2 - EARNINGS PER SHARE

The earnings per common share computations are based upon income applicable to common shares and the average number of shares of common stock, common stock equivalents (e.g., stock options, warrants and restricted stock) and potentially dilutive securities (e.g., convertible securities) outstanding, as adjusted for the Stock Split. The number of shares used in the primary earnings per share computations (before and after the extraordinary loss) for the three and nine months ended September 30, 1996 was 64,532,717 and 64,741,285, respectively. The number of shares used in the fully diluted earnings per share computations before the extraordinary loss for the three and nine months ended September 30, 1996 was 82,482,792 and 81,694,080, respectively. The number of shares used in the fully diluted earnings per share computations after the extraordinary loss for the three and nine months ended September 30, 1996 was 64,532,717 and 81,694,080, respectively. The number of shares used in the primary earnings per share computations for the three and nine months ended September 30, 1995 was 70,732,930 and 64,514,176, respectively. The number of shares used in the fully diluted earnings per share computations for the three and nine months ended September 30, 1995 was 81,939,622 and 68,249,740, respectively. Preferred stock dividend requirements decreased net income for these computations by \$1 million and \$3 million for the three and nine months ended September 30, 1996, respectively. In 1995, preferred stock dividend requirements, including accretion to redemption value and the accelerated accretion on the redeemed Series A 8% Cumulative Preferred Stock

caused by the exchange of such preferred stock for debt on September 29, 1995 decreased net income for these computations by \$5 million and \$8 million for the three and nine months ended September 30, 1995, respectively.

NOTE 3 - OPTION CONTRACTS

The Company has entered into petroleum option contracts to provide some short-term protection against a sharp increase in jet fuel prices, and the Company's 91%-owned subsidiary, Continental Micronesia, Inc. ("CMI"), has entered into average rate option contracts to hedge a portion of its Japanese yen-denominated ticket sales against a significant depreciation in the value of the yen versus the United States dollar. The petroleum option contracts generally cover the Company's forecasted jet fuel needs for approximately six months, and the average rate option contracts cover a portion of CMI's yen-denominated ticket sales for the next six to nine months. At September 30, 1996, the Company had petroleum option contracts outstanding with an aggregate notional value of \$226 million and CMI had average rate option contracts outstanding with a contract value of \$114 million. At September 30, 1996, the carrying value of the option contracts was immaterial. For the three and nine months ended September 30, 1996, the Company recognized fuel hedging gains totaling \$16 million and \$37 million, respectively.

The Company and CMI are exposed to credit loss in the event of nonperformance by the counterparties on the option contracts; however, management does not anticipate nonperformance by these counterparties. The amount of such exposure is generally the unrealized gains, if any, on such option contracts.

NOTE 4 - NONRECURRING CHARGES

During the third quarter of 1996, the Company made the decision to accelerate the replacement of 30 DC-9-30 aircraft, six DC-10-10 aircraft, 31 727-200 aircraft, 13 737-100 aircraft and 17 737-200 aircraft between August 1997 and December 1999. In connection with this decision, the Company placed two new aircraft orders with The Boeing Company ("Boeing"). As a result of its decision to accelerate the replacement of these aircraft, the Company recorded a nonrecurring charge of \$128 million. The nonrecurring charge relates primarily to (i) the writedown of Stage 2 aircraft inventory, which is not expected to be consumed through operations, to its estimated fair value; and (ii) a provision for costs associated with the return of leased aircraft at the end of their respective lease terms. The majority of the aircraft are being accounted for as operating leases and therefore, the Company will continue to recognize rent expense on these aircraft through the respective dates they are removed from service. Cash outlays of approximately \$54 million will be incurred in connection with costs associated with the return of the leased aircraft to the applicable lessors.

NOTE 5 - INCOME TAXES

Income taxes for the three and nine months ended September 30, 1996 are provided at the estimated effective tax rate. For the nine months ended September 30, 1996, the estimated effective tax rate differs from the federal statutory rate of 35%, primarily due to net operating losses ("NOLs") for which a tax benefit had not previously been recorded, and differs for the three months ended September 30, 1996 due to state and foreign income taxes and the effect of certain expenses that are not deductible for income tax purposes. Continental recognized the remainder of its previously unbenefitted post reorganization NOLs during the second quarter of 1996. A provision for income taxes was recorded in the second quarter of 1995 related to the System One Information Management, Inc. ("System One") transactions (see Note 6). No provision for income taxes was recorded for the three months ended September 30, 1995 and no additional provision was recorded for the nine months ended September 30, 1995 since the Company had incurred net operating losses for which a tax benefit had not previously been recorded.

At December 31, 1995, the Company had NOL carryforwards of \$2.6 billion for federal income tax purposes (of which \$1.3 billion are not subject to the limitations of Section 382 of the Internal Revenue Code ("Section 382")) that will expire from 1996 through 2009, and investment tax credit carryforwards of \$45 million that will expire through 2001. As a result of the change in ownership of the Company on April 27, 1993, the ultimate utilization of the Company's NOLs and investment tax credits could be limited.

For financial reporting purposes, a valuation allowance has been recognized to offset the deferred tax assets related to a portion of the NOLs. The Company has considered prudent and feasible tax planning strategies in assessing the need for the valuation allowance. The Company initially assumed \$194 million of benefit attributable to such tax planning strategies. The Company consummated the System One transactions, which had the effect of realizing approximately \$78 million of the built-in gains required to be realized, and currently intends to consummate one or more additional transactions. In the event the Company were to determine in the future that any such tax planning strategies would not be implemented, an adjustment to the net deferred tax liability of up to \$116 million would be charged to income in the period such determination was made. In the event the Company recognizes additional tax benefits related to NOLs and investment tax credit carryforwards attributable to the Company's predecessor, which include the accounts of Continental Airlines Holdings, Inc. and the pre-reorganized Company, those benefits would be applied to reduce reorganization value in excess of amounts allocable to identifiable assets and other intangibles to zero, and thereafter as an addition to paid-in capital.

NOTE 6 - OTHER

Financing Transactions

In the first and second quarters of 1996, the Company financed one owned aircraft and exercised its right under 22 existing leveraged aircraft leases to cause the owner/lessor's debt underlying these leases to be refinanced. In connection with these financings, the Company leased the aircraft through pass-through trusts ("Trusts") rather than directly from the equipment provider to reduce Continental's overall financing costs. The lower borrowing costs obtained in the refinancing allowed Continental's operating lease expense for the affected aircraft to be reduced by more than \$17 million annually. In connection with the refinancing, Trusts were created to hold new non-recourse equipment notes (with the exception that equipment notes with respect to one owned aircraft were issued by Continental). The Trusts issued pass-through certificates representing interests in the equipment notes. Inasmuch as (i) the owner/lessor has a substantial investment in the aircraft, (ii) the pass-through certificates are secured by the aircraft and an assignment of the corresponding leases and lease rentals payable by Continental, and (iii) the pass-through certificates are not direct obligations of, or guaranteed by, Continental, the Trusts (and the corresponding debt and interest expense) are not included in the accompanying consolidated financial statements. Continental has both renewal options and fair market value purchase options under the related aircraft leases.

During January and February 1996, the Company repurchased or redeemed without prepayment penalty the remaining amount of its Series A convertible secured debentures for \$125 million (including payment-in-kind interest of \$7 million).

In March 1996, Continental issued \$230 million of 6-3/4% convertible subordinated notes due April 15, 2006. The notes are convertible into Class B common stock at an initial conversion price of \$30.195 per share (adjusted for the Stock Split). The notes are redeemable at the option of the Company on or after April 15, 1999, at specified redemption prices.

In March 1996, Continental repaid \$257 million of secured indebtedness to General Electric Company and affiliates (collectively, "GE") (of which \$47 million was required as a result

of the convertible notes financing described above and the America West Airlines, Inc. ("America West") stock sale (discussed below) and \$210 million was an optional prepayment), which eliminated certain restrictive covenants.

In March 1996, the Company's wholly owned subsidiary, Continental Express, Inc. ("Express"), entered into an agreement to acquire eight new ATR aircraft. As of September 1996, five of these aircraft had been delivered. These aircraft are being accounted for as operating leases. In conjunction with the acquisition, the Company is returning eight older ATR aircraft accounted for as capital leases. As of September 1996, four of these aircraft had been returned.

In July 1996, CMI consummated a \$320 million secured term loan financing with a group of banks and other financial institutions. The loan was made in two tranches - a \$180 million five-year amortizing term loan with a floating interest rate of LIBOR plus 175 basis points and a \$140 million seven-year amortization extended loan with a floating interest rate of LIBOR plus 200 basis points. The loan is secured by the stock of CMI and substantially all of its unencumbered assets, consisting primarily of CMI's route authorities, and is guaranteed by Continental and Air Micronesia, Inc. ("AMI"), CMI's parent company.

CMI used the net proceeds of the financing to prepay \$160 million in principal amount of indebtedness to GE and to pay transaction costs, and Continental used the \$136 million in proceeds received by it as an indirect dividend from CMI, together with approximately \$28 million in cash on hand, to prepay \$164 million in principal amount of indebtedness to GE. In connection with the prepayment, Continental recorded a \$6 million after tax extraordinary loss relating to early extinguishment of debt.

The bank financing is expected to reduce interest expense by \$6 million in the first year, based on current rates. The bank financing does not contain any restrictive covenants at the Continental parent level, and none of the assets of the parent company (other than its stock in AMI) is pledged in connection with the financing. Accordingly, this transaction freed up over \$1 billion of collateral at Continental Airlines which was previously pledged under the terms of the GE debt agreements.

Continental CRS Interests, Inc. ("Continental CRS")

Continental and its subsidiary, System One, entered into a series of transactions on April 27, 1995 whereby a substantial portion of System One's assets (including the travel agent subscriber base and travel-related information management products and services software), as well as certain liabilities of System One, were transferred to a newly formed limited liability company, System One Information Management, L.L.C. ("LLC"). LLC is owned equally by Continental CRS (which was formerly named System One and remains a wholly owned subsidiary of Continental), Electronic Data Systems Corporation ("EDS") and AMADEUS, a European computerized reservation system ("CRS"). Substantially all of System One's remaining assets (including the CRS software) and liabilities were transferred to AMADEUS. In addition to the one-third interest in LLC, Continental CRS received cash proceeds of \$40 million and an equity interest in AMADEUS valued at \$120 million, and outstanding indebtedness of \$42 million of System One owed to EDS was extinguished. System One's revenues, included in cargo, mail and other revenue, and related net earnings are not material to the consolidated financial statements of Continental. In connection with these transactions, the Company recorded a pre-tax gain of \$108 million, which amount was included in other nonoperating income (expense) in the accompanying consolidated statement of operations for the nine months ended September 30, 1995. The related tax provision totaled \$78 million (which differs from the federal statutory rate due to certain nondeductible expenses), for a net gain of \$30 million.

Commitments

In July 1996, the Company announced its plan to expand its gates

and related facilities in Terminal B, as well as planned improvements at Terminal C, at Continental's Houston Intercontinental Airport hub. The expansion is expected to cost approximately \$115 million, which the Company expects will be funded principally by the issuance of tax-exempt debt by the applicable municipal authority. In connection therewith, the Company expects to enter into long-term leases (or amendments to existing leases) with the applicable municipal authority containing rental payments sufficient to service the related tax-exempt debt.

In October 1996, Continental placed an order for 60 firm 737-500 and 737-600 aircraft. See Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Other

In February 1996, the Company sold approximately 1.4 million shares of its 1.8 million shares of America West common stock in an underwritten public offering, realizing net proceeds of approximately \$25 million and recognizing a gain of \$12.5 million. In addition, in May 1996, the Company sold all of its 802,860 America West warrants held, realizing net proceeds of \$7 million and recognizing a gain of \$5 million. The gains are included in other nonoperating income. The Company currently owns approximately 1.0% of the equity interest and 7.9% of the voting power of America West.

On June 26, 1996, the stockholders of the Company approved an amendment to the Company's 1994 Incentive Equity Plan (as amended, the "Incentive Plan") which increased the maximum number of shares of Class B common stock that may be issued under the Incentive Plan from 6,000,000 to 9,000,000 shares, in the aggregate, on a post-Stock Split basis.

NOTE 7 - RELATED PARTY TRANSACTIONS

In May 1996, the Company entered into an agreement with Air Partners, L.P. ("Air Partners") for the sale by Air Partners to the Company from time to time, at Air Partners' election, for the one-year period beginning August 15, 1996, of up to an aggregate of \$50 million in intrinsic value (the then-current Class B common stock price minus exercise price) of Air Partners' Class B warrants. The purchase price would be payable in cash. The Board of Directors has authorized the Company to publicly issue up to \$50 million of Class B common stock in connection with any such purchase, and the Company has an effective registration statement covering such potential issuance. In connection with this agreement, the Company has reclassified \$50 million from common equity to redeemable warrants.

On May 14, 1996, Air Canada exchanged 1,661,056 shares of Class A common stock for 1,661,056 shares of Class B common stock (on a pre-Stock Split basis) pursuant to certain rights granted to it under the Company's Certificate of Incorporation.

In connection with the Company's \$320 million secured term loan financing (see Note 6), CMI paid its 9% minority interest holder, United Micronesia Development Association, Inc. ("UMDA"), a dividend of approximately \$13 million.

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

RESULTS OF OPERATIONS

The following discussion provides an analysis of the Company's results of operations and reasons for material changes therein for the three and nine months ended September 30, 1996 as compared to the three and nine months ended September 30, 1995.

The following information contains forward looking statements. Numerous important factors, including those factors identified as Risk Factors filed as Exhibit 99.1 hereto and incorporated herein by reference, and the fact that the assumptions filed as Exhibit 99.2 hereto and incorporated herein by reference relating to

certain of such forward looking statements could prove incorrect, could cause actual results to differ materially from those contained in such forward looking statements.

Comparison of Three Months Ended September 30, 1996 to Three Months Ended September 30, 1995

The Company recorded consolidated net income of \$18 million and \$111 million for the three months ended September 30, 1996 and 1995, respectively, including a \$128 million nonrecurring charge (\$77 million after taxes) and a \$6 million after tax extraordinary loss in 1996. Excluding the nonrecurring charge, the Company recorded income before income taxes, minority interest and extraordinary loss of \$175 million, an increase of 54.9%, \$62 million, from the same period in the prior year. Continental's financial and operating performance improved significantly in the third quarter of 1996 compared to the third quarter of 1995, reflecting, among other things, continued implementation of the Company's strategic program to enhance the fundamentals of its operations, rationalize capacity, improve customer service and employee relations and strengthen Continental's balance sheet and liquidity. Management believes that the Company benefitted significantly from the expiration of the aviation trust fund tax (the "ticket tax") on December 31, 1995, although the amount of any such benefit directly resulting from the expiration of the ticket tax cannot be precisely determined. The ticket tax was reimposed on August 27, 1996, and is again scheduled to expire on December 31, 1996. Management believes that the reimposition of the ticket tax has a negative impact on the Company, although the amount of such negative impact directly resulting from the reimposition of the ticket tax cannot be precisely determined.

Passenger revenue increased 10.3%, \$144 million, during the quarter ended September 30, 1996 as compared to the same period in 1995, primarily due to a 5.1% increase in revenue passenger miles and a 4.2% increase in the average yield per revenue passenger mile. The Company's capacity increased 5.3% during the third quarter of 1996 as compared to the comparable period in 1995, primarily due to increased utilization of existing aircraft.

Cargo, mail and other revenue increased 10.6%, \$12 million, in the three months ended September 30, 1996 as compared to the same period in the prior year, principally as a result of an agreement with DHL International to operate a sorting and distribution hub in Manila and an increase in charter revenue.

Wages, salaries and related costs increased 11.5%, \$41 million, during the quarter ended September 30, 1996 as compared to the same period in 1995, primarily due to pay increases effective July 1, 1996 for Continental's jet pilots and all non-unionized employees, an increase in base wages and per diem payments for flight attendants resulting from the Company's recently ratified collective bargaining agreement with the International Association of Machinists and Aerospace Workers ("IAM") representing Continental's flight attendants and additional costs associated with the Company's 5.3% increase in capacity over such period.

Aircraft fuel expense increased 17.5%, \$30 million, in the three months ended September 30, 1996 as compared to the same period in the prior year. The average price per gallon, net of fuel hedging gains of \$16 million, increased 9.5% from 54.88 cents in the third quarter of 1995 to 60.10 cents in the third quarter of 1996. In addition, there was a 6.3% increase in the quantity of jet fuel used from 303 million gallons in the third quarter of 1995 to 322 million gallons in the third quarter of 1996, principally reflecting increased capacity and stage lengths.

Commissions expense increased 7.1%, \$9 million, in the quarter ended September 30, 1996 as compared to the same period in the prior year, primarily due to a 10.3% increase in passenger revenue, offset by a decrease in the percentage of commissionable revenue.

Aircraft rentals increased 4.9%, \$6 million, for the three months ended September 30, 1996 compared to the same period in 1995, primarily as a result of the delivery of new aircraft throughout

1996. Such increase was partially offset by retirements of certain leased aircraft.

During the third quarter of 1996, the Company made the decision to accelerate the replacement of 30 DC-9-30 aircraft, six DC-10-10 aircraft, 31 727-200 aircraft, 13 737-100 aircraft and 17 737-200 aircraft between August 1997 and December 1999. In connection with this decision, the Company placed two new aircraft orders with Boeing. As a result of its decision to accelerate the replacement of these aircraft, the Company recorded a nonrecurring charge of \$128 million. The nonrecurring charge relates primarily to (i) the writedown of Stage 2 aircraft inventory, which is not expected to be consumed through operations, to its estimated fair value; and (ii) a provision for costs associated with the return of leased aircraft at the end of their respective lease terms.

Other operating expense increased 5.3%, \$17 million, in the three months ended September 30, 1996 as compared to the same period in the prior year, due primarily to increases in aircraft servicing, passenger services and fuel tax. Increased passenger services are a result of a 6.5% increase in block hours, and a 2.9% increase in revenue passengers.

Interest expense decreased 23.1%, \$12 million, during the three months ended September 30, 1996 as compared to the same period in 1995, primarily due to principal reductions of long-term debt and capital lease obligations and the reduced accretion of deferred credits recorded in connection with the Company's adjustment of operating leases to fair market value as of April 27, 1993.

The Company's other nonoperating income (expense) in the quarter ended September 30, 1996 includes a \$5 million payment to settle certain litigation arising out of the Company's decision in 1995 to cap domestic travel agency commissions. In addition, foreign currency losses (primarily related to the Japanese yen) were included in other nonoperating income (expense). Other nonoperating income (expense) in the third quarter of 1995 included a \$5 million charge which represented a waiver fee to a major creditor of the Company.

The income tax provision of \$18 million for the three months ended September 30, 1996 consists of federal, state and foreign income taxes. During the second quarter of 1996, the Company fully utilized previously unbenefitted post reorganization NOLs and began accruing income tax expense. No provision for federal income taxes was recorded for the three months ended September 30, 1995 as a result of the utilization of previously incurred NOLs for which a tax benefit had not previously been recorded.

In July 1996, an extraordinary loss of \$6 million was recorded, net of \$4 million income tax benefit, related to the early extinguishment of debt.

Comparison of Nine Months Ended September 30, 1996 to Nine Months Ended September 30, 1995

The Company recorded consolidated net income of \$272 million and \$183 million for the nine months ended September 30, 1996 and 1995, respectively, including a \$128 million nonrecurring charge (\$77 million after taxes) and a \$6 million after tax extraordinary loss in 1996. Continental's financial and operating performance improved significantly in the first nine months of 1996 compared to the first nine months of 1995, reflecting, among other things, continued implementation of the Company's strategic program to enhance the fundamentals of its operations, rationalize capacity, improve customer service and employee relations and strengthen its balance sheet and liquidity. Management believes that the Company benefitted significantly from the expiration of the ticket tax on December 31, 1995, although the amount of any such benefit directly resulting from the expiration of the ticket tax cannot be precisely determined. The ticket tax was reimposed on August 27, 1996, and is again scheduled to expire on December 31, 1996. Management believes that the reimposition of the ticket tax has a negative impact on the Company, although the amount of such negative impact directly resulting from the reimposition of the ticket tax cannot

be precisely determined.

Implementation of the Company's route realignment and capacity rationalization initiatives reduced capacity by 1.5% in the first nine months of 1996 as compared to the same period in 1995. This decrease in capacity, combined with a 3.3% increase in traffic, produced a 3.1 percentage point increase in load factor to 68.9%. This higher load factor, combined with a 6.6% increase in the average yield per revenue passenger mile, contributed to an 11.1% increase in passenger revenue to \$4.4 billion despite the decreased capacity.

Cargo, mail and other revenue decreased 11.4%, \$46 million, in the nine months ended September 30, 1996 as compared to the same period in the prior year, primarily as a result of the System One transactions (which were effective April 27, 1995). Partially offsetting such decrease was an increase in other revenue resulting from a wet lease agreement with Alitalia Airlines, an agreement with DHL International to operate a sorting and distribution hub in Manila and an increase in revenue related to military charters.

Wages, salaries and related costs increased 5.6%, \$60 million, during the nine months ended September 30, 1996 as compared to the same period in 1995. The increase is attributable to pay increases effective July 1, 1996 for Continental's jet pilots and all non-unionized employees and an increase in base wages and per diem payments for flight attendants resulting from the Company's collective bargaining agreement with the IAM representing Continental's flight attendants. In addition, there were increases in employee profit sharing accruals and the payment of bonuses for on-time airline performance.

Aircraft fuel expense increased 9.8%, \$50 million, in the nine months ended September 30, 1996 as compared to the same period in the prior year. The average price per gallon, net of fuel hedging gains of \$37 million, increased 9.5% from 53.98 cents in the first nine months of 1995 to 59.09 cents in the first nine months of 1996.

Commissions expense increased 5.9%, \$22 million, in the nine months ended September 30, 1996 as compared to the same period in the prior year, primarily due to an 11.1% increase in passenger revenue, partially offset by a decrease in the percentage of commissionable revenue.

Maintenance, materials and repairs increased 10.1%, \$32 million, during the nine months ended September 30, 1996 as compared to the same period in 1995, principally due to the volume and timing of engine overhauls as part of the Company's ongoing maintenance program.

Other rentals and landing fees decreased 4.8%, \$13 million, for the nine months ended September 30, 1996 compared to the same period in 1995, principally due to reduced facility rentals and landing fees resulting from capacity reductions.

During the third quarter of 1996, the Company made the decision to accelerate the replacement of 30 DC-9-30 aircraft, six DC-10-10 aircraft, 31 727-200 aircraft, 13 737-100 aircraft and 17 737-200 aircraft between August 1997 and December 1999. In connection with this decision, the Company placed two new aircraft orders with Boeing. As a result of its decision to accelerate the replacement of these aircraft, the Company recorded a nonrecurring charge of \$128 million. The nonrecurring charge relates primarily to (i) the writedown of Stage 2 aircraft inventory, which is not expected to be consumed through operations, to its estimated fair value; and (ii) a provision for costs associated with the return of leased aircraft at the end of their respective lease terms.

Other operating expense decreased 2.9%, \$29 million, in the nine months ended September 30, 1996 as compared to the same period in the prior year, primarily as a result of the System One transactions (which were effective April 27, 1995) and a decrease in advertising expense partially offset by increases in passenger services and fuel tax.

Interest expense decreased 20.4%, \$33 million, during the nine months ended September 30, 1996 as compared to the same period in 1995, primarily due to principal reductions of long-term debt and capital lease obligations and the reduced accretion of deferred credits recorded in connection with the Company's adjustment of operating leases to fair market value as of April 27, 1993.

Interest income increased 36.4%, \$8 million, in the first nine months of 1996 compared to the same period in the prior year, principally due to an increase in the average interest rate earned on investments coupled with an increase in the average invested balance of cash and cash equivalents.

The Company's other nonoperating income (expense) in the nine months ended September 30, 1996 includes a \$12.5 million gain related to the sale of approximately 1.4 million shares of America West common stock and a \$5 million gain related to the sale of the America West warrants. Other nonoperating income (expense) in the first nine months of 1995 consisted of a pre-tax gain of \$108 million from the System One transactions and a \$5 million pre-tax charge which represented a waiver fee to a major creditor of the Company.

The income tax provision for the nine months ended September 30, 1996 of \$57 million consists of federal, state and foreign income taxes. During the second quarter of 1996, the Company fully utilized previously unbenefitted post reorganization NOLs, and began accruing income tax expense. A provision for federal income taxes was recorded for the nine months ended September 30, 1995 related to the System One transactions. No additional provision was recorded due to the previously incurred NOLs for which a tax benefit had not previously been recorded.

In July 1996, an extraordinary loss of \$6 million was recorded, net of \$4 million income tax benefit, related to the early extinguishment of debt.

An analysis of statistical information for Continental's jet operations for the periods indicated is as follows:

	Three Months Ended September 30,		Net Increase/ (Decrease)
	1996	1995	
Revenue passenger miles (millions) (a)	11,302	10,757	5.1 %
Available seat miles (millions) (b)	16,117	15,312	5.3 %
Block hours (thousands) (c)	293	275	6.5 %
Passenger load factor (d)	70.1%	70.3%	(0.2) pts.
Breakeven passenger load factor (e)	61.0%	62.7%	(1.7) pts.
Passenger revenue per available seat mile (cents) (f)	8.95	8.61	3.9 %
Total revenue per available seat mile (cents) (g)	9.81	9.43	4.0 %
Operating cost per available seat mile (cents) (h), (l)	8.60	8.44	1.9 %
Operating cost per block hour (l)	\$4,731	\$4,690	0.9 %
Average yield per revenue passenger mile (cents) (i)	12.77	12.26	4.2 %
Average fare per revenue passenger	\$144.70	\$136.04	6.4 %
Revenue passengers (thousands)	9,972	9,695	2.9 %
Average length of aircraft flight (miles)	914	858	6.5 %
Average daily utilization of each aircraft (hours) (j)	10:10	9:45	4.3 %
Actual aircraft in fleet at end of period (k)	314	311	1.0 %

	Nine Months Ended September 30, 1996	September 30, 1995	Net Increase/ (Decrease)
Revenue passenger miles (millions) (a)	31,581	30,577	3.3 %
Available seat miles (millions) (b)	45,820	46,496	(1.5) %
Block hours (thousands) (c)	842	826	1.9 %
Passenger load factor (d)	68.9%	65.8%	3.1 pts.
Breakeven passenger load factor (e)	60.5%	61.1%	(0.6) pts.
Passenger revenue per available seat mile (cents) (f)	9.07	8.12	11.7 %
Total revenue per available seat mile (cents) (g)	9.94	8.91	11.6 %
Operating cost per available seat mile (cents) (h), (l)	8.77	8.27	6.0 %
Operating cost per block hour (l)	\$4,772	\$4,653	2.6 %
Average yield per revenue passenger mile (cents) (i)	13.16	12.34	6.6 %
Average fare per revenue passenger	\$143.97	\$131.98	9.1 %
Revenue passengers (thousands) . .	28,858	28,597	0.9 %
Average length of aircraft flight (miles)	893	831	7.5 %
Average daily utilization of each aircraft (hours) (j)	9:52	9:35	3.0 %
Actual aircraft in fleet at end of period (k)	314	311	1.0 %

- (a) The number of scheduled miles flown by revenue passengers.
- (b) The number of seats available for passengers multiplied by the number of scheduled miles those seats are flown.
- (c) The number of hours an aircraft is operated in revenue service from gate-to-gate.
- (d) Revenue passenger miles divided by available seat miles.
- (e) The percentage of seats that must be occupied by revenue passengers in order for the airline to break even on an income before income taxes basis, excluding nonrecurring charges, nonoperating items and other special items.
- (f) Passenger revenue divided by available seat miles.
- (g) Total revenue divided by available seat miles.
- (h) Operating expenses divided by available seat miles.
- (i) The average revenue received for each mile a revenue passenger is carried.
- (j) The average block hours flown per day in revenue service per aircraft.
- (k) 1996 excludes four all cargo 727 aircraft at CMI.
- (l) 1996 excludes nonrecurring charges totaling \$128 million.

LIQUIDITY AND CAPITAL COMMITMENTS

During the first nine months of 1996, the Company completed a number of transactions intended to strengthen its long-term financial position and enhance earnings. During January and February, Continental repurchased or redeemed without prepayment penalty the remaining amount of its Series A convertible secured debentures for \$125 million (including payment-in-kind interest of \$7 million). In February, Continental sold approximately 1.4 million of the 1.8 million shares it owned in America West, realizing net proceeds of approximately \$25 million and recognizing a gain of approximately \$12.5 million. In addition, in May, Continental sold all of its 802,860 America West warrants held, realizing net proceeds of approximately \$7 million and recognizing a gain of \$5 million. On March 26, Continental issued \$230 million of 6-3/4% convertible subordinated notes. The net proceeds from this offering and from the America West stock sale, as well as cash on hand, were used for the repayment of certain outstanding GE indebtedness totaling \$257 million (of which \$47 million was required as a result of the convertible notes financing and the America West stock sale and \$210 million was an optional

prepayment). In the first and second quarters, the Company financed one owned aircraft and exercised its right under 22 existing leveraged aircraft leases to cause the owner/lessor's debt underlying these leases to be refinanced. The lower borrowing costs obtained in the refinancing allowed Continental's operating lease expense for the affected aircraft to be reduced by more than \$17 million annually. In July, CMI consummated a \$320 million secured term loan financing with a group of banks and other financial institutions. Continental and CMI used the net proceeds, together with available cash, to prepay approximately \$324 million in principal amount of GE indebtedness. The bank financing is expected to reduce interest expense by \$6 million in the first year, based on current rates. The bank financing does not contain any restrictive covenants at the Continental parent level, and none of the assets of the parent company (other than its stock in AMI) is pledged in connection with the financing. Accordingly, this transaction freed up over \$1 billion of collateral at Continental Airlines which was previously pledged under the terms of the GE debt agreements. See Note 6.

As a result of NOLs, the Company will not pay United States federal income taxes (other than alternative minimum tax) until it has recorded approximately an additional \$1.3 billion of taxable income following December 31, 1995. Section 382 imposes limitations on a corporation's ability to utilize NOLs if it experiences an "ownership change". In general terms, an ownership change may result from transactions increasing the ownership of certain stockholders in the stock of a corporation by more than 50 percentage points over a three-year period. The sale of the Company's common stock in April 1996 pursuant to an underwritten public offering arranged by the Company (the "Secondary Offering") gave rise to an increase in percentage ownership by certain stockholders for this purpose. The Company believes that such percentage increase did not give rise to an ownership change under Section 382 as a result of the Secondary Offering. However, no assurance can be given that future transactions, whether within or outside the control of the Company, will not cause a change in ownership, thereby substantially limiting the potential utilization of the NOLs in a given future year. In the event that an ownership change should occur, utilization of Continental's NOLs would be subject to an annual limitation under Section 382 determined by multiplying the value of the Company's stock (including both common and preferred stock) at the time of the ownership change by the applicable long-term tax exempt rate (which was 5.63% for September 1996). Unused annual limitation may be carried over to later years, and the amount of the limitation may under certain circumstances be increased by the built-in gains in assets held by the Company at the time of the change that are recognized in the five-year period after the change. Under current conditions, if an ownership change were to occur, Continental's NOL utilization would be limited to approximately \$100 million per year.

Continental had firm commitments with Boeing to take delivery of 43 new jet aircraft during the years 1997 through 2002. During the third quarter of 1996, Continental amended the terms of its commitments with Boeing to take delivery of a total of 61 jet aircraft during the years 1997 through 2003 with options for an additional 23 aircraft. These amendments changed the aircraft mix and timing of delivery of aircraft, in order to more closely match Continental's anticipated future aircraft needs. In addition, in October 1996, Continental placed an order for 60 firm 737-500 and 737-600 aircraft that will replace older, less efficient Stage 2 aircraft between August 1997 and December 1999. The estimated aggregate cost of the Company's firm commitment Boeing aircraft is in excess of \$4 billion. The Company has commitments of approximately \$1.4 billion of backstop financing for its Boeing aircraft orders. Continental currently plans to finance the indebtedness on its new aircraft using enhanced equipment trust certificates or similar financing, subject to availability and market conditions. However, further financing will be needed to satisfy the Company's capital commitments for new Boeing aircraft. There can be no assurance that sufficient financing will be available for all aircraft and other capital expenditures not covered by firm financing commitments. The Company has also entered into agreements with several outside parties to lease four

DC-10-30 aircraft and to purchase three DC-10-30 aircraft and two MD-82 aircraft. These nine aircraft are expected to be delivered during the period from October 1996 through mid-year 1997, and the Company expects to finance the aircraft to be purchased from available cash or from third party sources.

In addition, in March 1996, Express entered into an agreement to acquire eight new ATR aircraft. As of September 1996, five of these aircraft had been delivered. The aircraft are being accounted for as operating leases. In conjunction with the acquisition, the Company is returning eight older ATR aircraft accounted for as capital leases. As of September 1996, four of these aircraft had been returned. Also, in September 1996, Express announced an order for 25 firm EMB-145 50-seat regional jets with options for an additional 175 aircraft. Express plans to account for these aircraft as operating leases. Neither Express nor Continental will have any obligation to take aircraft which are not financed by a third party and leased to Express. Continental will guarantee Express' obligations under the operating leases. Express will take delivery of the 25 firm aircraft during the period from December 1996 through the third quarter of 1998.

Continental expects its cash outlays for 1996 capital expenditures, exclusive of aircraft acquisitions, to aggregate \$120 million, primarily relating to mainframe, software application and automation infrastructure projects, aircraft modifications and mandatory maintenance projects, passenger terminal facility improvements and office, maintenance, telecommunications and ground equipment. Continental's capital expenditures during the nine months ended September 30, 1996 aggregated \$93 million, exclusive of aircraft acquisitions.

The Company expects to fund its future capital commitments through internally generated funds, together with general Company financings and aircraft financing transactions. However, there can be no assurance that sufficient financing will be available for all aircraft and other capital expenditures not covered by firm financing commitments.

In July 1996, the Company announced its plan to expand its gates and related facilities in Terminal B, as well as planned improvements at Terminal C, at Continental's Houston Intercontinental Airport hub. The expansion is expected to cost approximately \$115 million, which the Company expects will be funded principally by the issuance of tax-exempt debt by the applicable municipal authority. In connection therewith, the Company expects to enter into long-term leases (or amendments to existing leases) with the applicable municipal authority containing rental payments sufficient to service the related tax-exempt debt.

As of September 30, 1996, the Company had \$865 million in cash and cash equivalents, compared to \$747 million as of December 31, 1995. Net cash provided by operating activities increased \$330 million during the nine months ended September 30, 1996 compared to the same period in the prior year principally due to earnings improvement. Net cash used by investing activities for the nine months ended September 30, 1996 compared to the same period in the prior year increased \$220 million, primarily as a result of higher capital expenditures in 1996, lower purchase deposits refunded in connection with aircraft delivered in 1996 and proceeds received in 1995 in connection with the System One transactions. This increase was offset in part by proceeds received from the sale in 1996 of approximately 1.4 million shares of Continental's America West stock and all of Continental's America West warrants. Net cash used by financing activities increased \$199 million primarily due to the repayment of long-term debt, using in part the proceeds received from the issuance of the 6-3/4% convertible subordinated notes, dividends paid on preferred securities of trust and a dividend paid to UMDA in connection with the \$320 million secured term loan financing.

Continental does not have general lines of credit and has significant encumbered assets.

Approximately \$70 million and \$144 million of cash and cash

equivalents at September 30, 1996 and December 31, 1995, respectively, were held in restricted arrangements relating primarily to workers' compensation claims and in accordance with the terms of certain other agreements. The \$320 million financing consummated by CMI in July 1996 contains significant financial covenants relating to CMI, including maintenance of a minimum fixed charge coverage ratio, a minimum consolidated net worth and minimum liquidity, and covenants restricting CMI's leverage, its incurrence of certain indebtedness and its pledge of assets. The financial covenants also limit the ability of CMI to pay dividends to Continental.

CMI entered into an interest rate swap agreement and an interest rate cap agreement to reduce the impact of potential increases in interest rates on its bank financing that was completed in July 1996. The interest rate swap agreement effectively converts the floating rate on the bank financing to a fixed rate of 5.875%. The notional value on the interest rate swap agreement is \$320 million and is effective from August 30, 1996 through January 30, 1997. The interest rate cap agreement has a notional value of \$153 million and is effective from January 31, 1997 through July 31, 2001.

The Company has entered into petroleum option contracts to provide some short-term protection against a sharp increase in jet fuel prices, and CMI has entered into average rate option contracts to hedge a portion of its Japanese yen-denominated ticket sales against a significant depreciation in the value of the yen versus the United States dollar. The petroleum option contracts generally cover the Company's forecasted jet fuel needs for approximately three to six months, and the average rate option contracts cover a portion of CMI's yen-denominated ticket sales for the next six to nine months. At September 30, 1996, the Company had petroleum option contracts outstanding with an aggregate notional value of \$226 million and CMI had average rate option contracts outstanding with a contract value of \$114 million. At September 30, 1996, the carrying value of the option contracts was immaterial. The Company and CMI are exposed to credit loss in the event of nonperformance by the counterparties on the option contracts; however, management does not anticipate nonperformance by these counterparties. The amount of such exposure is generally the unrealized gains, if any, on such option contracts.

In August 1996, the IAM representing the Company's Continental Airlines unit flight attendants ratified a three and one-half year collective bargaining agreement which will remain in effect for 42 months beginning June 24, 1996. The agreement provides for base wage increases in each year of the contract, a one-time adjustment to certain base wage scales as an equitable adjustment, an increase in per diem payments and other matters, including productivity improvements. In addition, effective July 1, 1996, Continental implemented pay increases for substantially all of its non-unionized employees as part of a three-year plan to increase base wages to be more comparable to industry wages. The Company anticipates that the pay increases for Continental's flight attendants and its non-unionized employees will result in a cumulative increase in wages, salaries and related costs (assuming no change in the Company's operations) of \$137 million through 1999 (approximately \$15 million through the remainder of 1996, \$67 million through 1997, \$107 million through 1998 and \$137 million through 1999). In addition, under the Company's existing collective bargaining agreement with the union representing its jet pilots, those pilots received a 13.5% wage increase on July 1, 1996 and will receive a 5% wage increase on June 30, 1997. The Company anticipates that it will be able to offset a significant portion of these wage and other cost increases with increased labor productivity, reduced interest and lease expenses, reduced distribution costs and other cost savings.

Continental's decision to order 60 new Boeing 737-500 and 737-600 aircraft to replace older, less efficient aircraft is expected to increase ownership costs while generating cost savings in the areas of maintenance, fuel and pilot training. The Company estimates net pre-tax savings from the order to approximate \$28 million, \$31 million, \$66 million, \$115 million and \$116 million in the years

1997 through 2001, respectively. See the assumptions filed herewith as Exhibit 99.2.

Management also believes that the Company's costs are likely to be affected for the remainder of 1996 by (i) higher aircraft rental expense as new aircraft are delivered, (ii) changes in the costs of materials and services (in particular, the cost of fuel, which can fluctuate significantly in response to global market conditions), (iii) changes in governmental regulations and taxes affecting air transportation and the costs charged for airport access, including new security requirements, (iv) changes in the Company's fleet and related capacity and (v) the Company's continuing efforts to reduce costs throughout its operations, including reduced maintenance costs for new aircraft, reduced distribution expense from using E-Ticket and the Internet for bookings and reduced interest expense.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

On December 3, 1990, the Company owned 77 aircraft and 81 spare engines (in four collateral pools) securing debt evidenced by equipment trust certificates. The trustees for the four collateral pools moved in the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court") for "adequate protection" payments under Sections 361 and 363 of the federal bankruptcy code for the Company's retention and use of the aircraft and engines after December 3, 1990, including postpetition claims for the alleged decline in market value of the aircraft and engines after December 3, 1990 and claims for deterioration in the condition of the aircraft and engines in the same period. The Bankruptcy Court rejected the adequate protection claims that alleged market value decline. Prior to April 16, 1993, the Company settled all of the adequate protection claims of the trustees, except for a claim of approximately \$117 million for alleged market value decline of 29 aircraft and 81 spare engines in the fourth collateral pool. On April 16, 1993, the Bankruptcy Court rejected the market value decline claims of the trustees for the fourth collateral pool in their entirety and incorporated those findings into its order confirming the Plan of Reorganization. The trustees for the fourth collateral pool appealed from these orders, but failed to obtain a stay pending appeal. The Company opposed these appeals on the merits and sought dismissal of the appeals on the grounds they were made moot by the substantial consummation of the Plan of Reorganization. The United States District Court for the District of Delaware (the "District Court") dismissed the appeals as moot, and the trustees appealed to the Third Circuit Court of Appeals (the "Third Circuit") seeking review of the District Court's mootness determination and the Bankruptcy Court's finding on the merits. The Third Circuit affirmed the District Court's dismissal in February 1996, but subsequently granted a rehearing en banc on May 14, 1996. On July 31, 1996, the Third Circuit, acting en banc, also affirmed the District Court's dismissal. The trustees may apply for a writ of certiorari to the U.S. Supreme Court. The Company does not believe that the foregoing matter will have a material adverse effect on the Company.

In September 1996, the Company signed a settlement agreement providing for the settlement of all claims against it in consolidated antitrust litigation in the U.S. District Court for the District of Minnesota. Continental, along with various other airlines, has been a defendant in that litigation since February 1995. Plaintiffs in that litigation claim that Continental and the other airline defendants conspired to fix and maintain the commissions paid to U.S. travel agents for domestic travel. Plaintiffs claim substantial damages, which would be trebled under applicable antitrust law. While denying all claims, Continental determined to settle the litigation to avoid the risks and expenses of further litigation. The settlement, which is subject to Court approval, includes the payment by Continental of approximately \$5 million and provides for the complete release of all claims and dismissal of the case against the Company.

ITEM 2. CHANGES IN SECURITIES.

On June 26, 1996, the Board of Directors of the Company declared a two-for-one stock split for its Class A and Class B common stock. See Item 1. "Financial Statements. Note 1 - Stock Split" for information with respect to the stock split.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits filed herewith:

- 3.1 Amended By-Laws of the Company.
- 10.1* Amendment to employment agreement, dated as of September 30, 1996, between the Company and Gordon M. Bethune.
- 10.2* Amendment to employment agreement, dated as of September 30, 1996, between the Company and Gregory D. Brenneman.
- 10.3* Form of amendment to employment agreement, dated as of September 30, 1996, for each of Lawrence W. Kellner, C. D. McLean and Barry P. Simon.
- 10.4* Third Amendment to Continental Airlines, Inc. 1994 Incentive Equity Plan.
- 11.1 Statement Regarding Computation of Per Share Earnings.
- 27.1 Financial Data Schedule.
- 99.1 Risk Factors.
- 99.2 Assumptions relating to pre-tax savings from new Boeing order.

(b) Reports on Form 8-K:

- (i) Report dated July 22, 1996, reporting an Item 5. "Other Event". No financial statements were filed with the report which announced the prepayment of approximately \$324 million in principal amount of indebtedness to affiliates of General Electric Company.
- (ii) Report dated September 16, 1996 reporting an Item 5. "Other Event". No financial statements were filed with the report which announced that Lloyd M. Bentsen had been elected to the Company's Board of Directors.
- (iii) Report dated September 30, 1996 reporting an Item 5. "Other Event". No financial statements were filed with the report which announced that Gordon M. Bethune had been elected as Chairman of the Board and Chief Executive Officer of the Company, that Gregory D. Brenneman had been elected as President and Chief Operating Officer of the Company, and that David Bonderman had resigned as Chairman of the Board of the Company.

*These exhibits relate to management contracts or compensatory plans or arrangements.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CONTINENTAL AIRLINES, INC.
(Registrant)

Date: October 21, 1996 by: /s/ Lawrence W. Kellner
Lawrence W. Kellner
Senior Vice President and
Chief Financial Officer
(On behalf of Registrant)

Date: October 21, 1996 /s/ Michael P. Bonds
Michael P. Bonds
Vice President and Controller
(Chief Accounting Officer)

BY-LAWS
OF
CONTINENTAL AIRLINES, INC.

Including all amendments through September 30, 1996

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OF

CONTINENTAL AIRLINES, INC.

Incorporated under the Laws of the State of Delaware

ARTICLE I

Stockholders

Section 1.1 Annual Meeting. The annual meeting of stockholders of the Corporation for the election of Directors and for the transaction of any other proper business shall be held at such time and date in each year as the Board of Directors may determine from time to time. The annual meeting in each year shall be held at such place within or without the State of Delaware as may be fixed by the Board of Directors, or if not so fixed, at the principal business office of the Corporation.

Section 1.2 Special Meetings. Subject to the rights of the holders of any class or series of preferred stock of the Corporation, or any other series or class of stock as set forth in the Restated Certificate of Incorporation of the Corporation (as it may be amended from time to time in accordance with its terms and applicable law, the "Restated Certificate of Incorporation"), to elect additional Directors under specified circumstances, special meetings of the stockholders may be called only by (i) stockholders holding Common Stock constituting more than 50% of the voting power of the outstanding shares of Common Stock, (ii) the Chief Executive Officer or (iii) the Board of Directors.

Section 1.3 Place of Meeting. The Board of Directors may designate the place of meeting for any meeting of the stockholders. If no designation is made by the Board of Directors, the place of meeting shall be the principal executive offices of the Corporation.

Section 1.4 Notice of Meetings. Whenever stockholders are required or permitted to take any action at a meeting, unless notice is waived in writing by all stockholders entitled to vote at the meeting, a written notice of the meeting shall be given which shall state the place, date and hour of the meeting, and, in the case of a special meeting, the purpose for which the meeting is called.

Unless otherwise provided by law, and except as to any stockholder duly waiving notice, the written notice of any meeting shall be given personally or by mail, not less than ten nor more than 60 days before the date of the meeting to each stockholder entitled to vote at such meeting. If mailed, notice shall be deemed given when deposited in the mail, postage prepaid, directed to the stockholder at his or her address as it appears on the records of the Corporation.

When a meeting is adjourned to another time or place, notice need not be given of the adjourned meeting if the time and place thereof are announced at the meeting at which the adjournment is taken. At the adjourned meeting the Corporation may transact any business which might have been transacted at the original meeting. If, however, the adjournment is for more than 30 days, or if after the adjournment a new record date is fixed for the adjourned meeting, a notice of the adjourned meeting shall be given to each stockholder of record entitled to vote at the meeting.

Section 1.5 Quorum. Except as otherwise provided by law, by the Restated Certificate of Incorporation, or by these By-Laws in respect of the vote required for a specified action, at any meeting of stockholders the holders of a majority of the aggregate voting power of the outstanding stock entitled to vote thereat, either present or represented by proxy, shall constitute a quorum for the transaction of any business, but the stockholders present, although less than a quorum, may adjourn the meeting to another time or place and, except as provided in the last paragraph of Section 1.4, notice need not be given of the adjourned meeting.

Section 1.6 Voting. Except as otherwise provided by the Restated Certificate of Incorporation or these By-Laws, whenever Directors are to be elected at a meeting, they shall be elected by a plurality of the votes cast at the meeting by the holders of stock entitled to vote. Whenever any corporate action, other than

the election of Directors, is to be taken by vote of stockholders at a meeting, it shall be authorized by a majority of the votes cast at the meeting by the holders of stock entitled to vote thereon, except as otherwise required by law, by the Restated Certificate of Incorporation or by these By-Laws.

Except as otherwise provided by law, or by the Restated Certificate of Incorporation or these By-Laws, each holder of record of stock of the Corporation entitled to vote on any matter at any meeting of stockholders shall be entitled to one vote for each share of such stock standing in the name of such holder on the stock ledger of the Corporation on the record date for the determination of the stockholders entitled to vote at the meeting.

Upon the demand of any stockholder entitled to vote, the vote for Directors or the vote on any other matter at a meeting shall be by written ballot, but otherwise the method of voting and the manner in which votes are counted shall be discretionary with the presiding officer at the meeting.

Section 1.7 Presiding Officer and Secretary. At every meeting of stockholders the Chairman of the Board or the Chief Executive Officer, as designated by the Board of Directors, or, if neither is present, or in the absence of any such designation, the appointee of the meeting, shall preside. The Secretary, or in his or her absence an Assistant Secretary, or if none be present, the appointee of the presiding officer of the meeting, shall act as secretary of the meeting.

Section 1.8 Proxies. Each stockholder entitled to vote at a meeting of stockholders may authorize another person or persons to act for him or her by proxy executed in writing by the stockholder or as otherwise permitted by law, or by his or her duly authorized attorney-in-fact. Such proxy must be filed with the Secretary of the Corporation or his or her representative at or before the time of the meeting.

Section 1.9 List of Stockholders. The officer who has charge of the stock ledger of the Corporation shall prepare and make, at least ten days before every meeting of stockholders, a complete list of the stockholders entitled to vote at the meeting, arranged in alphabetical order, and showing the address of each stockholder and the number of shares registered in the name of each stockholder. Such list shall be open to the examination of any stockholder, for any purpose germane to the meeting, during ordinary business hours, for a period of at least ten days prior to the meeting, either at a place within the city where the meeting is to be held, which place shall be specified in the notice of the meeting, or, if not so specified, at the place where the meeting is to be held. The list shall also be produced and kept at the time and place of the meeting during the whole time thereof, and may be inspected by any stockholder who is present.

The stock ledger shall be the only evidence as to which stockholders are the stockholders entitled to examine the stock ledger or the list required by this Section 1.9, or to vote in person or by proxy at any meeting of stockholders.

Section 1.10 Notice of Stockholder Business and Nominations.

(A) Annual Meetings of Stockholders. (1) Subject to Section 2.2 of these By-Laws, nominations of persons for election to the Board of Directors of the Corporation and the proposal of business to be considered by the stockholders may be made at an annual meeting of stockholders (a) pursuant to the Corporation's notice of meeting delivered pursuant to Section 1.4 of these By-Laws, (b) by or at the direction of the Board of Directors or (c) by any stockholder of the Corporation who is entitled to vote at the meeting, who complied with the notice procedures set forth in clauses (2) and (3) of paragraph (A) of this Section 1.10 and who was a stockholder of record at the time such notice is delivered to the Secretary of the Corporation.

(2) For nominations or other business to be properly brought before an annual meeting by a stockholder pursuant to clause (c) of paragraph (A) (1) of this Section 1.10, the stockholder must have given timely notice thereof in writing to the Secretary of the Corporation. To be timely, a stockholder's notice shall be delivered to the Secretary at the principal executive offices of the Corporation not less than seventy days nor more than ninety days prior to the first anniversary of the preceding year's annual meeting; provided, however, that in the event that the date of the annual meeting is advanced by more than twenty days, or delayed by more than seventy days, from such anniversary date,

notice by the stockholder to be timely must be so delivered not earlier than the ninetieth day prior to such annual meeting and not later than the close of business on the later of the seventieth day prior to such annual meeting or the tenth day following the day on which public announcement of the date of such meeting is first made. Such stockholder's notice shall set forth (a) as to each person whom the stockholder proposes to nominate for election or reelection as a Director all information relating to such person that is required to be disclosed in solicitations of proxies for election of Directors, or is otherwise required, in each case pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), including such person's written consent to being named in the proxy statement as a nominee and to serving as a Director if elected; (b) as to any other business that the stockholder proposes to bring before the meeting, a brief description of the business desired to be brought before the meeting, the reasons for conducting such business at the meeting and any material interest in such business of such stockholder and the beneficial owner, if any, on whose behalf the proposal is made; and (c) as to the stockholder giving the notice and the beneficial owner, if any, on whose behalf the nomination or proposal is made (i) the name and address of such stockholder, as they appear on the Corporation's books, and of such beneficial owner and (ii) the class and number of shares of the Corporation which are owned beneficially and of record by such stockholder and such beneficial owner.

(3) Notwithstanding anything in the second sentence of paragraph (A) (2) of this Section 1.10 to the contrary, in the event that the number of Directors to be elected to the Board of Directors is increased and there is no public announcement naming all of the nominees for Director or specifying the size of the increased Board of Directors made by the Corporation at least eighty days prior to the first anniversary of the preceding year's annual meeting, a stockholder's notice required by this Section 1.10 shall also be considered timely, but only with respect to nominees for any new positions created by such increase, if it shall be delivered to the Secretary at the principal executive offices of the Corporation not later than the close of business on the tenth day following the day on which such public announcement is first made by the Corporation.

(B) Special Meeting of Stockholders. Only such business shall be conducted at a special meeting of stockholders as shall have been brought before the meeting pursuant to the Corporation's notice of meeting pursuant to Section 1.4 of these By-Laws. Subject to Section 2.2 of these By-Laws, nominations of persons for election to the Board of Directors may be made at a special meeting of stockholders at which Directors are to be elected pursuant to the Corporation's notice of meeting (i) by or at the direction of the Board of Directors or (ii) by any stockholder of the Corporation who is entitled to vote at the meeting, who complies with the notice procedures set forth in this Section 1.10 and who is a stockholder of record at the time such notice is delivered to the Secretary of the Corporation. Nominations by stockholders of persons for election to the Board of Directors may be made at such a special meeting of stockholders if the stockholder's notice as required by paragraph (A) (2) of this Section 1.10 shall be delivered to the Secretary at the principal executive offices of the Corporation not earlier than the ninetieth day prior to such special meeting and not later than the close of business on the later of the seventieth day prior to such special meeting or the tenth day following the day on which public announcement is first made of the date of the special meeting and of the nominees proposed by the Board of Directors to be elected at such meeting.

(C) General. (1) Only persons who are nominated in accordance with the procedures set forth in this Section 1.10 shall be eligible to serve as Directors and only such business shall be conducted at a meeting of stockholders as shall have been brought before the meeting in accordance with the procedures set forth in this Section 1.10. Except as otherwise provided by law, the Restated Certificate of Incorporation or these By-Laws, the chairman of the meeting shall have the power and duty to determine whether a nomination or any business proposed to be brought before the meeting was made in accordance with the procedures set forth in this Section 1.10 and, if any proposed nomination or business is not in compliance with this Section 1.10, to declare that such

defective proposal or nomination shall be disregarded.

(2) For purposes of this Section 1.10, "public announcement" shall mean disclosure in a press release reported by the Dow Jones News Service, Associated Press or comparable national news service or in a document publicly filed by the Corporation with the Securities and Exchange Commission pursuant to Section 13, 14 or 15(d) of the Exchange Act.

(3) Notwithstanding the foregoing provisions of this Section 1.10, a stockholder shall also comply with all applicable requirements of the Exchange Act and the rules and regulations thereunder with respect to the matters set forth in this Section 1.10. Nothing in this Section 1.10 shall be deemed to affect any rights of stockholders to request inclusion of proposals in the Corporation's proxy statement pursuant to Rule 14a-8 under the Exchange Act.

Section 1.11 Inspectors of Elections; Opening and Closing the Polls. The Board of Directors by resolution shall appoint one or more inspectors, which inspector or inspectors may include individuals who serve the Corporation in other capacities, including, without limitation, as officers, employees, agents or representatives of the Corporation, to act at the meeting and make a written report thereof. One or more persons may be designated as alternate inspectors to replace any inspector who fails to act. If no inspector or alternate has been appointed to act, or if all inspectors or alternates who have been appointed are unable to act, at the meeting of stockholders, the chairman of the meeting shall appoint one or more inspectors to act at the meeting. Each inspector, before discharging his or her duties, shall take and sign an oath faithfully to execute the duties of inspector with strict impartiality and according to the best of his or her ability. The inspectors shall have the duties prescribed by the General Corporation Law of the State of Delaware (the "GCL").

The chairman of the meeting shall fix and announce at the meeting the time of the opening and the closing of the polls for each matter upon which the stockholders will vote at a meeting.

ARTICLE II

Directors

Section 2.1 Powers and Duties of Directors; Number. The business of the Corporation shall be managed by or under the direction of the Board of Directors, which may exercise all such powers of the Corporation and do all such lawful acts and things as are not directed or required to be exercised or done by the stockholders by the Restated Certificate of Incorporation, by these By-Laws, or by law. Except as otherwise permitted by or consistent with Foreign Ownership Restrictions (as defined in the Restated Certificate of Incorporation), at no time shall more than one-third of the Directors in office be Aliens (as defined in the Restated Certificate of Incorporation). The Board shall adopt the Annual Capital Expenditure Budget and the Annual Financial Plan, both as defined in Section 3.3, for each fiscal year not later than the last day of the preceding fiscal year or at such later time as shall be determined by resolution of the Board.

The number of Directors which shall constitute the whole Board of Directors shall be determined from time to time by resolution of the Board of Directors (provided that no decrease in the number of Directors which would have the effect of shortening the term of an incumbent Director may be made by the Board of Directors). If the Board of Directors makes no such determination, the number of Directors shall be twelve.

Section 2.2 Election; Term; Vacancies. Each Director shall hold office until the next annual election and until his or her successor is elected and qualified, or until his earlier death, resignation or removal. The Directors shall be elected annually by the stockholders in the manner specified by the Restated Certificate of Incorporation and these By-Laws, except that if there be a vacancy in the Board of Directors by reason of death, resignation or otherwise, such vacancy may also be filled for the unexpired term by a majority affirmative vote of the Board of Directors; provided, that in the event of a vacancy by reason of death, resignation or otherwise of a Class D Director, such vacancy shall be filled for the unexpired term by the holders of Class D Common Stock, voting separately as a class by a majority affirmative vote thereof.

Section 2.3 Resignation. Any Director may resign at any time upon written notice to the Corporation. Any such resignation

shall take effect at the time specified therein or, if the time be not specified, upon receipt thereof, and the acceptance of such resignation, unless required by the terms thereof, shall not be necessary to make such resignation effective.

Section 2.4 Removal. Any Director may be removed at any time, with or without cause, by vote at a meeting or written consent of the holders of stock entitled to vote on the election of such Director pursuant to the Restated Certificate of Incorporation.

Section 2.5 Meetings.

(A) Annual Meeting. Immediately after each annual meeting of stockholders, the duly elected Directors shall hold an inaugural meeting for the purpose of organization, election of officers, and the transaction of other business, at such place as shall be fixed by the person presiding at the meeting of stockholders at which such Directors are elected.

(B) Regular Meetings. Regular meetings of the Board of Directors shall be held on such dates and at such times and places as shall be designated from time to time by the Board of Directors; provided, that regular meetings of the Board of Directors can be waived at the request of the Chief Executive Officer if at least a majority of the Directors agree in writing to such waiver at least seven days before the date of the meeting to be so waived. The Secretary shall forward to each Director, at least five days before any such regular meeting, a notice of the time and place of the meeting, together with the agenda for the meeting or in lieu thereof a notice of waiver if the regular meeting has been waived.

(C) Special Meetings. Special meetings of the Directors may be called by the Chairman of the Board, the Chairman of the Executive Committee, the Chief Executive Officer or a majority of the Directors, at such time and place as shall be specified in the notice or waiver thereof. Notice of each special meeting, including the time and place of the meeting and the agenda therefor, shall be given by the Secretary or by the person calling the meeting to each Director by causing the same to be delivered personally or by facsimile transmission not later than the close of business on the second day next preceding the day of the meeting.

(D) Location; Methods of Participation. Meetings of the Board of Directors, regular or special, may be held at any place within or without the State of Delaware at such place as is indicated in the notice or waiver of notice thereof. Members of the Board of Directors, or of any committee designated by the Board, may participate in a meeting of the Board of Directors or such committee by means of conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other, and participation in a meeting by such means shall constitute presence in person at such meeting.

Section 2.6 Quorum and Voting. A majority of the total number of Directors (excluding those who must recuse themselves under the terms of the Restated Certificate of Incorporation or these By-Laws, or by law) ("Recused Directors") shall constitute a quorum for the transaction of business, but, if there be less than a quorum at any meeting of the Board of Directors, a majority of the Directors present may adjourn the meeting from time to time, and no further notice thereof need be given other than announcement at the meeting which shall be so adjourned. Except as otherwise provided by law, by the Restated Certificate of Incorporation, or by these By-Laws, the affirmative vote of a majority of the Directors present at a meeting (excluding Recused Directors) at which a quorum is present shall be the act of the Board of Directors.

Section 2.7 Written Consent of Directors in Lieu of a Meeting. Any action required or permitted to be taken at any meeting of the Board of Directors or of any committee thereof may be taken without a meeting if all members of the Board or of such committee, as the case may be, consent thereto in writing, and the writing or writings are filed with the minutes of proceedings of the Board or committee.

Section 2.8 Compensation. Directors may receive compensation for services to the Corporation in their capacities as Directors or otherwise in such manner and in such amounts as may be fixed from time to time by the Board of Directors.

ARTICLE III

Committees of the Board of Directors

Section 3.1 Creation. The Board of Directors, by resolution or resolutions passed by a majority of the whole Board of Directors (except as otherwise provided in the Restated Certificate of Incorporation), may designate one or more committees, each to consist of such number of Directors of the Corporation as shall be specified in such resolution; provided, that for so long as there shall be any Class D Directors (as defined in Section 3.3), any such committee shall include (if so requested by any Class D Director), to the extent consistent with applicable laws and regulations, such number of Class D Directors as shall not be greater than the number of Directors equal to the same percentage of the Directors comprising such committee as the percentage of the total number of Class D Directors on the whole Board of Directors; provided further, that for so long as there shall be any Class D Directors, any executive or other similar committee of the Board with full power to take all actions which may lawfully be taken by the Board, and any nominating committee of the Board, shall consist, to the extent consistent with applicable laws and regulations, only of a Director that is an officer of the Corporation (or his or her designee) and a Class D Director. Each committee of the Board shall have and may exercise such powers and duties as may be provided in such resolution, except that no such committee shall have the power to elect Directors or the power or authority reserved for the whole Board of Directors pursuant to Section 141(c)(1) of the GCL, except as otherwise set forth in such Section 141(c)(1). Pursuant to and subject to the foregoing, the Board of Directors shall at all times designate an Executive Committee with full power to take all actions which may lawfully be taken by the Board, and the chairperson of the Executive Committee shall, as long as Air Partners (as defined in the Restated Certificate of Incorporation) may convert (or has converted) shares of Class A common stock of the Corporation into Class D common stock of the Corporation pursuant to Article Fourth, Section 2(e)(i) of the Restated Certificate of Incorporation and such Class D common stock would not then be (or has not been) converted into Class A common stock pursuant to Article Fourth, Section 2(e)(ii) or (iii) of the Restated Certificate of Incorporation, be appointed from among the members of such committee by a majority of the whole Board of Directors.

Section 3.2 Committee Procedure. Each committee of the Board of Directors shall meet at the times stated by the Board in the resolution or resolutions establishing such committee or on notice to all members given by any member of such committee. The Board by resolution or resolutions shall establish the rules of procedure to be followed by each committee, which shall include a requirement that such committee keep regular minutes of its proceedings and deliver to the Secretary the same. The affirmative vote of a majority of the members of any such committee shall constitute the act of such committee.

Section 3.3 Certain Definitions.

(A) Annual Capital Expenditure Budget. When used in these By-Laws, the term "Annual Capital Expenditure Budget" shall mean an annual capital expenditure budget, which shall be approved by the Board of Directors not later than the last day of the preceding fiscal year (or at such later time determined by the Board pursuant to Section 2.1).

(B) Annual Financial Plan. When used in these By-Laws, the term "Annual Financial Plan" shall mean an annual financial plan, which shall be approved by the Board of Directors not later than the last day of the preceding fiscal year (or at such later time determined by the Board pursuant to Section 2.1).

(C) Class D Director. When used in these By-Laws, the term "Class D Director" shall mean a Director elected by the holders of Class D Common Stock or elected by Directors to fill a vacancy created by the departure of a Class D Director.

ARTICLE IV

Officers, Agents and Employees

Section 4.1 Appointment and Term of Office. The officers of the Corporation shall include a Chairman of the Board, a Chief Executive Officer, a President, and a Secretary, and may also include a Chief Operating Officer, a Treasurer, one or more Vice Presidents (who may be further classified by such descriptions as "executive", "senior", "assistant", "staff" or otherwise, as the Board of Directors shall determine), one or more Assistant

Secretaries and one or more Assistant Treasurers. All such officers shall be appointed by the Board of Directors. Any number of such offices may be held by the same person, but no officer shall execute, acknowledge or verify any instrument in more than one capacity. Except as may be prescribed otherwise by the Board of Directors in a particular case, all such officers shall hold their offices at the pleasure of the Board for an unlimited term and need not be reappointed annually or at any other periodic interval. The Board of Directors may appoint, and may delegate power to appoint, such other officers, agents and employees as it may deem necessary or proper, who shall hold their offices or positions for such terms, have such authority and perform such duties as may from time to time be determined by or pursuant to authorization of the Board of Directors.

Section 4.2 Resignation and Removal. Any officer may resign at any time upon written notice to the Corporation. Any officer, agent or employee of the Corporation may be removed by the Board of Directors with or without cause at any time. The Board of Directors may delegate such power of removal as to officers, agents and employees not appointed by the Board of Directors. Such removal shall be without prejudice to a person's contract rights, if any, but the appointment of any person as an officer, agent or employee of the Corporation shall not of itself create contract rights.

Section 4.3 Compensation and Bond. The compensation of the officers of the Corporation shall be fixed by the Board of Directors, but this power may be delegated to any officer by the Board of Directors. The Corporation may secure the fidelity of any or all of its officers, agents or employees by bond or otherwise.

Section 4.4 Chairman of the Board. The Chairman of the Board shall be selected from the members of the Board of Directors and shall preside at all meetings of the Board of Directors. In addition, the Chairman of the Board shall have such other powers and duties as may be delegated to him or her by the Board of Directors. The Chairman of the Board shall not be deemed to be an officer of the Corporation for purposes of Article III of these By-Laws unless he or she shall also be the Chief Executive Officer.

Section 4.5 Chief Executive Officer. The Chief Executive Officer shall be the chief executive officer of the Corporation and, in the absence of the Chairman of the Board (or if there be none), he or she shall preside at all meetings of the Board of Directors. The Chief Executive Officer shall have general charge of the business affairs of the Corporation. He or she may employ and discharge employees and agents of the Corporation, except such as shall be appointed by the Board of Directors, and he or she may delegate these powers. The Chief Executive Officer may vote the stock or other securities of any other domestic or foreign corporation of any type or kind which may at any time be owned by the Corporation, may execute any stockholders' or other consents in respect thereof and may in his or her discretion delegate such powers by executing proxies, or otherwise, on behalf of the Corporation. The Board of Directors by resolution from time to time may confer like powers upon any other person.

Section 4.6 President. The President shall have such powers and perform such duties as the Board of Directors or the Chief Executive Officer may from time to time prescribe.

Section 4.7 Chief Operating Officer. The Chief Operating Officer of the Company shall have general charge of the operating affairs of the Corporation, and shall have such other powers and duties as the Chief Executive Officer or the Board of Directors shall delegate to him or her from time to time.

Section 4.8 Vice Presidents. Each Vice President shall have such powers and perform such duties as the Board of Directors or the Chief Executive Officer may from time to time prescribe.

Section 4.9 Treasurer. The Treasurer shall have charge of all funds and securities of the Corporation, may endorse the same for deposit or collection when necessary and deposit the same to the credit of the Corporation in such banks or depositories as the Board of Directors may authorize. He or she may endorse all commercial documents requiring endorsements for or on behalf of the Corporation and may sign all receipts and vouchers for payments made to the Corporation. He or she shall have all such further powers and duties as generally are incident to the position of Treasurer or as may be assigned to him or her by the Board of Directors or the Chief Executive Officer.

Section 4.10 Secretary. The Secretary shall distribute all materials to be distributed in connection with regular and special meetings of the Board of Directors, record all the proceedings of the meetings of the stockholders and Directors in a book to be kept for that purpose and shall also record therein all action taken by written consent of the Directors, and committees of the Board of Directors in lieu of a meeting. He or she shall attend to the giving and serving of all notices of the Corporation. He or she shall have custody of the seal of the Corporation and shall attest the same by his or her signature whenever required. He or she shall have charge of the stock ledger and such other books and papers as the Board of Directors may direct, but he or she may delegate responsibility for maintaining the stock ledger to any transfer agent appointed by the Board of Directors. He or she shall have all such further powers and duties as generally are incident to the position of Secretary or as may be assigned to him or her by the Board of Directors or the Chief Executive Officer.

Section 4.11 Assistant Treasurers. In the absence or inability to act of the Treasurer, any Assistant Treasurer may perform all the duties and exercise all the powers of the Treasurer. The performance of any such duty shall, in respect of any other person dealing with the Corporation, be conclusive evidence of his or her power to act. An Assistant Treasurer shall also perform such other duties as the Treasurer or the Board of Directors may assign to him or her.

Section 4.12 Assistant Secretaries. In the absence or inability to act of the Secretary, any Assistant Secretary may perform all the duties and exercise all the powers of the Secretary. The performance of any such duty shall, in respect of any other person dealing with the Corporation, be conclusive evidence of his or her power to act. An Assistant Secretary shall also perform such other duties as the Secretary or the Board of Directors may assign to him or her.

Section 4.13 Delegation of Duties. In case of the absence of any officer of the Corporation, or for any other reason that the Board of Directors may deem sufficient, the Board of Directors may confer for the time being the powers or duties, or any of them, of such officer upon any other officer or upon any Director.

Section 4.14 Loans to Officers and Employees; Guaranty of Obligations of Officers and Employees. The Corporation may lend money to, or guarantee any obligation of, or otherwise assist any officer or other employee of the Corporation or any subsidiary, including any officer or employee who is a Director of the Corporation or any subsidiary, whenever, in the judgment of the Directors, such loan, guaranty or assistance may reasonably be expected to benefit the Corporation. The loan, guaranty or other assistance may be with or without interest, and may be unsecured, or secured in such manner as the Board of Directors shall approve, including, without limitation, a pledge of shares of stock of the Corporation.

ARTICLE V Indemnification

Section 5.1 Indemnification of Directors, Officers, Employees and Agents. No Director of the Corporation shall be personally liable to the Corporation or its stockholders for monetary damages for breach of fiduciary duty as a Director, except for liability (i) for any breach of the Director's duty of loyalty to the corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) under Section 174 of the GCL, or (iv) for any transaction from which the Director derived any improper personal benefit. If the GCL is amended to authorize corporate action further eliminating or limiting the personal liability of Directors, then the liability of Directors of the Corporation shall be eliminated or limited to the full extent permitted by the GCL, as so amended.

The Corporation shall indemnify to the full extent permitted by the laws of the State of Delaware as from time to time in effect any person who was or is a party or is threatened to be made a party to, or otherwise requires representation by counsel in connection with, any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (whether or not an action by or in the right of the Corporation), by reason of the fact that he or she is or was a Director or officer of the Corporation, or, while serving as a

Director or officer of the Corporation, is or was serving at the request of the Corporation as a Director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, or by reason of any action alleged to have been taken or omitted in such capacity. The right to indemnification conferred by this Article V also shall include the right of such persons to be paid in advance by the Corporation for their expenses (including attorneys' fees) to the full extent permitted by the laws of the State of Delaware, as from time to time in effect. The right to indemnification conferred on such persons by this Article V shall be a contract right.

Unless otherwise determined by the Board of Directors, the Corporation shall indemnify to the full extent permitted by the laws of the State of Delaware as from time to time in effect any person who was or is a party or is threatened to be made a party to, or otherwise requires representation by counsel in connection with, any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (whether or not an action by or in the right of the Corporation), by reason of the fact that he or she is or was an employee (other than an officer) or agent of the Corporation, or is or was serving at the request of the Corporation as a Director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, or by reason of any action alleged to have been taken or omitted in such capacity.

The rights and authority conferred in this Article V shall not be exclusive of any other right which any person seeking indemnification or advancement of expenses may have or hereafter acquire under any statute, provision of the Restated Certificate of Incorporation or these By-Laws, agreement, vote of stockholders or disinterested Directors or otherwise, both as to action in his or her official capacity and as to action in another capacity while holding such office and shall continue as to a person who has ceased to be a Director, officer, employee or agent and shall inure to the benefit of the heirs, executors and administrators of such a person. Neither the amendment or repeal of this Article V nor the adoption of any provision of the Restated Certificate of Incorporation or these By-Laws or of any statute inconsistent with this Article V shall eliminate or reduce the effect of this Article V in respect of any acts or omissions occurring prior to such amendment, repeal or adoption or an inconsistent provision.

ARTICLE VI Common Stock

Section 6.1 Certificates. Certificates for stock of the Corporation shall be in such form as shall be approved by the Board of Directors and shall be signed in the name of the Corporation by the Chairman of the Board or the Chief Executive Officer or the President or a Vice President, and by the Treasurer or an Assistant Treasurer, or the Secretary or an Assistant Secretary. Such certificates may be sealed with the seal of the Corporation or a facsimile thereof. Any of or all the signatures on a certificate may be a facsimile. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer, transfer agent or registrar before such certificate is issued, it may be issued by the Corporation with the same effect as if he or she were such officer, transfer agent or registrar at the date of issue.

Section 6.2 Transfers of Stock. Upon surrender to any transfer agent of the Corporation of a certificate for shares of the Corporation duly endorsed or accompanied by proper evidence of succession, assignment or authority to transfer, it shall be the duty of the Corporation, provided such succession, assignment or transfer is not prohibited by the Restated Certificate of Incorporation, these By-Laws, applicable law or contractual prohibitions, to issue a new certificate to the person entitled thereto, cancel the old certificate and record the transaction upon its books.

Section 6.3 Lost, Stolen or Destroyed Certificates. The Corporation may issue a new stock certificate in the place of any certificate theretofore issued by it, alleged to have been lost, stolen or destroyed, and the Corporation may require the owner of the lost, stolen or destroyed certificate or his or her legal representative to give the Corporation a bond sufficient to indemnify it against any claim that may be made against it on

account of the alleged loss, theft or destruction of any such certificate or the issuance of any such new certificate. The Board of Directors may require such owner to satisfy other reasonable requirements.

Section 6.4 Stockholder Record Date. In order that the Corporation may determine the stockholders entitled to notice of or to vote at any meeting of stockholders or any adjournment thereof, or to express consent to corporate action in writing without a meeting, or entitled to receive payment of any dividend or other distribution or allotment of any rights, or entitled to exercise any rights in respect of any change, conversion or exchange of stock, or for the purpose of any other lawful action, the Board of Directors may fix, in advance, a record date, which shall not be more than 60 nor less than ten days before the date of such meeting, nor more than 60 days prior to any other action. Only such stockholders as shall be stockholders of record on the date so fixed shall be entitled to notice of, and to vote at, such meeting and any adjournment thereof, or to give such consent, or to receive payment of such dividend or other distribution, or to exercise such rights in respect of any such change, conversion or exchange of stock, or to participate in such action, as the case may be, notwithstanding any transfer of any stock on the books of the Corporation after any record date so fixed.

If no record date is fixed by the Board of Directors, (a) the record date for determining stockholders entitled to notice of or to vote at a meeting of stockholders shall be at the close of business on the day next preceding the date on which notice is given, or, if notice is waived by all stockholders entitled to vote at the meeting, at the close of business on the day next preceding the day on which the meeting is held and (b) the record date for determining stockholders for any other purpose shall be at the close of business on the day on which the Board of Directors adopts the resolution relating thereto.

A determination of stockholders of record entitled to notice of or to vote at a meeting of stockholders shall apply to any adjournment of the meeting; provided, however, that the Board of Directors may fix a new record date for the adjourned meeting.

ARTICLE VII

Ownership by Aliens

Section 7.1 Foreign Stock Record. There shall be maintained a separate stock record, designated the "Foreign Stock Record," for the registration of Voting Stock, as defined in Section 7.2, that is Beneficially Owned (as defined in the Restated Certificate of Incorporation) by Aliens, as defined in the Restated Certificate of Incorporation ("Alien Stock"). The Beneficial Ownership by Aliens of Voting Stock shall be determined in conformity with regulations prescribed by the Board of Directors.

Section 7.2 Maximum Percentage. At no time shall ownership of shares representing more than the Maximum Percentage, as defined below, be registered in the Foreign Stock Record. As used herein, (a) "Maximum Percentage" means the maximum percentage of voting power of Voting Stock, as defined below, which may be voted by, or at the direction of, Aliens without violating Foreign Ownership Restrictions or adversely affecting the Corporation's operating certificates or authorities, and (b) "Voting Stock" means all outstanding shares of capital stock of the Corporation issued from time to time by the Corporation and Beneficially Owned by Aliens which, but for the provisions of Section 1 of Article Sixth of the Restated Certificate of Incorporation, by their terms may vote (at the time such determination is made) for the election of Directors of the Corporation, except shares of Preferred Stock that are entitled to vote for the election of Directors solely as a result of the failure to pay dividends by the Corporation or other breach of the terms of such Preferred Stock.

Section 7.3 Recording of Shares. If at any time there exist shares of Voting Stock that are Alien Stock but that are not registered in the Foreign Stock Record, the Beneficial Owner thereof may request, in writing, the Corporation to register ownership of such shares on the Foreign Stock Record and the Corporation shall comply with such request, subject to the limitation set forth in Section 7.2. The order in which Alien Stock shall be registered on the Foreign Stock Record shall be chronological, based on the date the Corporation received a written request to so register such shares of Alien Stock; provided, that for so long as any transferee of Air Partners is an Alien, shares

of Voting Stock held by such transferee which were originally acquired by Air Partners pursuant to the Investment Agreement, dated as of November 9, 1992, as amended, among the Corporation, Air Canada and Air Partners (the "Investment Agreement"), or upon conversion or exchange of such securities, or as a dividend or distribution in respect of such securities (collectively "AP Original Equity Securities") shall be registered on the Foreign Ownership Record prior to, and to the exclusion of, any other shares of Alien Stock whether or not any such other shares of Alien Stock are registered on the Foreign Stock Record at the time that any such transferee of Air Partners requests that shares of AP Original Equity Securities be so registered. If at any time the Corporation shall find that the combined voting power of Voting Stock then registered in the Foreign Stock Record exceeds the Maximum Percentage, there shall be removed from the Foreign Stock Record the registration of such number of shares so registered as is sufficient to reduce the combined voting power of the shares so registered to an amount not in excess of the Maximum Percentage. The order in which such shares shall be removed shall be reverse chronological order based upon the date the Corporation received a written request to so register such shares of Alien Stock; provided, that for so long as any transferee of Air Partners is an Alien, shares of AP Original Equity Securities owned by such transferee shall not be removed from the Foreign Ownership Record (regardless of the date on which such shares were registered thereon) until all other outstanding shares of Alien Stock have been so removed.

ARTICLE VIII

General Provisions

Section 8.1 Fiscal Year. The fiscal year of the Corporation shall begin the first day of January and end on the last day of December of each year.

Section 8.2 Dividends. Dividends upon the capital stock may be declared by the Board of Directors at any regular or special meeting and may be paid in cash or in property or in shares of the capital stock. Before paying any dividend or making any distribution of profits, the Directors may set apart out of any funds of the Corporation available for dividends a reserve or reserves for any proper purpose and may alter or abolish any such reserve or reserves.

Section 8.3 Checks, Notes, Drafts, Etc. Checks, notes, drafts, acceptances, bills of exchange and other orders or obligations for the payment of money shall be signed by such officer or officers or person or persons as the Board of Directors or a duly authorized committee thereof, the Chief Executive Officer or the Treasurer may from time to time designate.

Section 8.4 Corporate Seal. The seal of the Corporation shall be circular in form and shall bear, in addition to any other emblem or device approved by the Board of Directors, the name of the Corporation, the year of its incorporation and the words "Corporate Seal" and "Delaware." The seal may be used by causing it or a facsimile thereof to be impressed or affixed or in any other manner reproduced.

Section 8.5 Waiver of Notice. Whenever notice is required to be given by statute, or under any provision of the Restated Certificate of Incorporation or these By-Laws, a written waiver thereof, signed by the person entitled to notice, whether before or after the time stated therein, shall be deemed equivalent to notice. In the case of a stockholder, such waiver of notice may be signed by such stockholder's attorney or proxy duly appointed in writing. Attendance of a person at a meeting shall constitute a waiver of notice of such meeting, except when the person attends a meeting for the express purpose of objecting at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened. Neither the business to be transacted at, nor the purpose of, any regular or special meeting of the stockholders, Directors or members of a committee of Directors need be specified in any written waiver of notice.

ARTICLE IX

Restated Certificate of Incorporation to Govern

Section 9.1 Restated Certificate of Incorporation to Govern. Notwithstanding anything to the contrary herein, if any provision contained herein is inconsistent with or conflicts with a provision of the Restated Certificate of Incorporation, such provision herein shall be superseded by the inconsistent provision

in the Restated Certificate of Incorporation, to the extent necessary to give effect to such provision in the Restated Certificate of Incorporation.

AMENDMENT TO EMPLOYMENT AGREEMENT

This Amendment to Employment Agreement (this "Amendment") is made by and between Continental Airlines, Inc., a Delaware corporation ("Company"), and Gordon M. Bethune ("Executive").

WITNESSETH:

WHEREAS, Company and Executive are parties to that certain Amended and Restated Employment Agreement dated as of November 15, 1995, as amended by Amendment to Employment Agreement dated as of April 19, 1996 (the "Existing Agreement"); and

WHEREAS, the Human Resources Committee of the Board of Directors of the Company, on September 30, 1996, authorized the execution and delivery on behalf of the Company of this Amendment; and

WHEREAS, Company and Executive desire to amend the Existing Agreement as hereinafter set forth;

NOW, THEREFORE, for and in consideration of the mutual promises, covenants and obligations contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Company and Executive agree as follows:

1. Paragraph 4.7(iv) of the Existing Agreement is hereby amended to read in its entirety as follows:

"(iv) "Termination Payment" shall mean an amount equal to three times the sum of (1) Executive's annual base salary pursuant to paragraph 3.1 in effect immediately prior to Executive's termination of employment hereunder and (2) a deemed annual bonus which shall be equal to the Bonus Percentage of the amount described in clause (1) of this paragraph 4.7(iv). The "Bonus Percentage" shall be a percentage equal to the annual percentage of base salary (i.e., 0% to 125%) paid or payable to a participant under the Company's Executive Bonus Program (and its predecessor or any successor plan or program) with respect to the most recent fiscal year ended prior to Executive's termination of employment; provided that, with respect to fiscal year 1996 only, no amount attributable to the 25% cash bonus paid January 2, 1996 and approved by the Human Resources Committee of the Board of Directors of the Company at its meeting on November 2, 1995 shall be included in the Bonus Percentage."

2. The Existing Agreement, as amended by this Amendment, is hereby ratified and confirmed and shall continue in full force and effect in accordance with its terms.

IN WITNESS WHEREOF, the parties hereto have executed this Amendment as of the 30th day of September, 1996.

CONTINENTAL AIRLINES, INC.

By: _____
Name:
Title:

EXECUTIVE

Gordon M. Bethune

AMENDMENT TO EMPLOYMENT AGREEMENT

This Amendment to Employment Agreement (this "Amendment") is made by and between Continental Airlines, Inc., a Delaware corporation ("Company"), and Gregory D. Brenneman ("Executive").

WITNESSETH:

WHEREAS, Company and Executive are parties to that certain Amended and Restated Employment Agreement dated as of November 15, 1995, as amended by Amendment to Employment Agreement dated as of April 19, 1996 (the "Existing Agreement"); and

WHEREAS, the Human Resources Committee of the Board of Directors of the Company, on September 30, 1996, authorized the execution and delivery on behalf of the Company of this Amendment; and

WHEREAS, Company and Executive desire to amend the Existing Agreement as hereinafter set forth;

NOW, THEREFORE, for and in consideration of the mutual promises, covenants and obligations contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Company and Executive agree as follows:

1. The first sentence of Paragraph 1.2 of the Existing Agreement is hereby amended to read in its entirety as follows:

"From and after September 30, 1996, Company shall employ Executive in the position of President and Chief Operating Officer of Company, or in such other position or positions as the parties may mutually agree."

2. A new sentence is hereby added as the last sentence of Paragraph 1.3 of the Existing Agreement as follows:

"Company shall, during the term of this Agreement, disclose or entrust trade secrets or confidential information to Executive, shall provide Executive the opportunity to develop business good will, or shall disclose or entrust business opportunities to Executive."

3. Paragraph 4.7(iv) of the Existing Agreement is hereby amended to read in its entirety as follows:

"(iv) "Termination Payment" shall mean an amount equal to three times the sum of (1) Executive's annual base salary pursuant to paragraph 3.1 in effect immediately prior to Executive's termination of employment hereunder and (2) a deemed annual bonus which shall be equal to the Bonus Percentage of the amount described in clause (1) of this paragraph 4.7(iv). The "Bonus Percentage" shall be a percentage equal to the annual percentage of base salary (i.e., 0% to 125%) paid or payable to a participant under the Company's Executive Bonus Program (and its predecessor or any successor plan or program) with respect to the most recent fiscal year ended prior to Executive's termination of employment; provided that, with respect to fiscal year 1996 only, no amount attributable to the 25% cash bonus paid January 2, 1996 and approved by the Human Resources Committee of the Board of Directors of the Company at its meeting on November 2, 1995 shall be included in the Bonus Percentage."

4. A new Paragraph 4.8 is hereby added to the Existing Agreement to read in its entirety as follows:

"4.8 Covenant Not to Compete. As part of the consideration for the compensation and benefits to be paid to Executive hereunder, in keeping with Executive's duties as a fiduciary, and to protect the trade secrets and confidential information

of Company that will be disclosed to Executive, the business goodwill of Company that will be developed in Executive, or the business opportunities that will be disclosed or entrusted to Executive by Company, Company and Executive agree to the non-competition provisions of this paragraph 4.8. Executive agrees that during the period of Executive's non-competition obligations hereunder, Executive will not, directly or indirectly for Executive or others, in any State, territory or protectorate of the United States in which Company is qualified to do business or in any foreign country in which Company has an office, station or branch as of the date of termination of Executive's employment with the Company, engage in an executive capacity in any business competitive with the business conducted by Company at the date of such termination.

These non-competition obligations shall extend through June 6, 1999. These non-competition obligations shall terminate and be inapplicable, however, if Executive's employment with the Company is terminated (A) by Company pursuant to paragraph 2.2(v), (B) by Executive pursuant to paragraphs 2.3(i), (ii), (iii), (iv), (v), or (vi), or (C) for any reason whatsoever following the occurrence of a Change in Control (as such term is defined in the Incentive Plan, as amended by the Board of Directors on April 19, 1996 and in effect on such date)."

5. The Existing Agreement, as amended by this Amendment, is hereby ratified and confirmed and shall continue in full force and effect in accordance with its terms.

IN WITNESS WHEREOF, the parties hereto have executed this Amendment as of the 30th day of September, 1996.

CONTINENTAL AIRLINES, INC.

By: _____
Name:
Title:

EXECUTIVE

Gregory D. Brenneman

AMENDMENT TO EMPLOYMENT AGREEMENT

This Amendment to Employment Agreement (this "Amendment") is made by and between Continental Airlines, Inc., a Delaware corporation ("Company"), and _____ ("Executive").

WITNESSETH:

WHEREAS, Company and Executive are parties to that certain Amended and Restated Employment Agreement dated as of November 15, 1995, as amended by Amendment to Employment Agreement dated as of April 19, 1996 (the "Existing Agreement"); and

WHEREAS, the Human Resources Committee of the Board of Directors of the Company, on September 30, 1996, authorized the execution and delivery on behalf of the Company of this Amendment; and

WHEREAS, Company and Executive desire to amend the Existing Agreement as hereinafter set forth;

NOW, THEREFORE, for and in consideration of the mutual promises, covenants and obligations contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Company and Executive agree as follows:

1. Paragraph 4.7(i) of the Existing Agreement is hereby amended to read in its entirety as follows:

"(i) "Annualized Compensation" shall mean an amount equal to the sum of (1) Executive's annual base salary pursuant to paragraph 3.1 in effect immediately prior to Executive's termination of employment hereunder and (2) a deemed annual bonus which shall be equal to the Bonus Percentage of the amount described in clause (1) of this paragraph 4.7(i). The "Bonus Percentage" shall be a percentage equal to the annual percentage of base salary (i.e., 0% to 125%) paid or payable to a participant under the Company's Executive Bonus Program (and its predecessor or any successor plan or program) with respect to the most recent fiscal year ended prior to Executive's termination of employment; provided that, with respect to fiscal year 1996 only, no amount attributable to the 25% cash bonus paid January 2, 1996 and approved by the Human Resources Committee of the Board of Directors of the Company at its meeting on November 2, 1995 shall be included in the Bonus Percentage."

2. The Existing Agreement, as amended by this Amendment, is hereby ratified and confirmed and shall continue in full force and effect in accordance with its terms.

IN WITNESS WHEREOF, the parties hereto have executed this Amendment as of the 30th day of September, 1996.

CONTINENTAL AIRLINES, INC.

By: _____
Name:
Title:

EXECUTIVE

EXHIBIT 10.4

THIRD AMENDMENT TO
CONTINENTAL AIRLINES, INC.
1994 INCENTIVE EQUITY PLAN

The Board of Directors of Continental Airlines, Inc., at a meeting held on September 30, 1996, adopted the following resolution amending the Continental Airlines, Inc. 1994 Incentive Equity Plan, as amended:

NOW THEREFORE, BE IT RESOLVED that, pursuant to the authority granted to this Board under Paragraph 15 of the Company's 1994 Incentive Equity Plan, as amended (the "Plan"), the first clause of Paragraph 5 of the Plan, and clause (a) of Paragraph 5 of the Plan, are hereby amended to read in their entirety as follows:

"5. Outside Director Stock Options. Notwithstanding any other provision of the Plan, (A) each Outside Director shall automatically receive on the day of each annual stockholders meeting (and, if such director is first elected to the Board after September 1, 1996 other than at an annual stockholders meeting, on the later of (i) the date of such director's first election to the Board or (ii) September 30, 1996) a grant of options to purchase 5,000 shares of Common Stock, and (B) each Outside Director who was elected as a director of the Company on June 26, 1996 shall automatically receive, on September 30, 1996 (which shall be the date of grant thereof), a grant of options to purchase 2,000 shares of Common Stock, in each case in accordance with the following provisions:

(a) The Committee and Board shall have no discretion with respect to Outside Director Stock Options. Each grant will be made with an Option Price equal to 100% of the Market Value per Share on the date of grant thereof."

CONTINENTAL AIRLINES, INC.
STATEMENT REGARDING COMPUTATION OF PER SHARE EARNINGS (1) (2)
(In thousands of dollars, except per share data)

	Three Months Ended September 30, 1996	Nine Months Ended September 30, 1996
Primary:		
Weighted average shares outstanding	53,423,575	53,190,790
Dilutive effect of outstanding stock options, warrants and restricted stock grants (as determined by the application of the treasury stock method)	11,109,142	11,550,495
Weighted average number of common shares outstanding, as adjusted	64,532,717	64,741,285
Income before extraordinary loss applicable to common shares	\$ 22,704	\$ 275,530
Add interest expense associated with the assumed reduction of borrowings, net of federal income tax effect	-	-
Income before extraordinary loss, as adjusted	\$ 22,704	\$ 275,530
Per share amount	\$ 0.35	\$ 4.26

(1) On June 26, 1996, the Board of Directors of the Company declared a two-for-one stock split (the "Stock Split") pursuant to which (a) one share of the Company's Class A common stock, par value \$.01 per share, was issued for each share of Class A common stock outstanding on July 2, 1996 (the "Record Date") and (b) one share of the Company's Class B common stock, par value \$.01 per share, was issued for each

share of Class B common stock outstanding on the Record Date. Shares issuable pursuant to the Stock Split were distributed on or about July 16, 1996. All share and earnings per share information for prior periods has been adjusted for the Stock Split.

(2) Excludes extraordinary net loss on early extinguishment of debt of \$6.3 million.

CONTINENTAL AIRLINES, INC.
STATEMENT REGARDING COMPUTATION OF PER SHARE EARNINGS (1)
(In thousands of dollars, except per share data)

Three Months Ended September 30, 1996	1995	Nine Months Ended September 30, 1996	1995
---------------------------------------------	------	--------------------------------------------	------

Primary:				
Weighted average shares outstanding	53,423,575	52,101,304	53,190,790	51,555,420
Dilutive effect of outstanding stock options, warrants and restricted stock grants (as determined by the application of the treasury stock method)	11,109,142	18,631,626	11,550,495	12,958,756
Weighted average number of common shares outstanding, as adjusted.	64,532,717	70,732,930	64,741,285	64,514,176
Income applicable to common shares	\$ 16,424	\$ 105,876	\$ 269,250	\$ 174,642
Add interest expense associated with the assumed reduction of borrowings, net of federal income tax effect	-	3,273	-	14,673
Income, as adjusted	\$ 16,424	\$ 109,149	\$ 269,250	\$ 189,315
Per share amount.	\$ 0.25	\$ 1.54	\$ 4.16	\$ 2.93

(1) On June 26, 1996, the Board of Directors of the Company declared a two-for-one stock split (the "Stock Split") pursuant to which (a) one share of the Company's Class A common stock, par value \$.01 per share, was issued for each share of Class A common stock outstanding on July 2, 1996 (the "Record Date") and (b) one share of the Company's Class B common stock, par value \$.01 per share, was issued for each share of Class B common stock outstanding on the Record Date. Shares issuable pursuant to the Stock Split were distributed on or about July 16, 1996. All share and earnings per share information for prior periods has been adjusted for the Stock Split.

Exhibit 11.1
Page 3 of 6

CONTINENTAL AIRLINES, INC.
STATEMENT REGARDING COMPUTATION OF PER SHARE EARNINGS (1) (2)
(In thousands of dollars, except per share data)

	Three Months Ended September 30, 1996	Nine Months Ended September 30, 1996
Fully diluted:		
Weighted average shares outstanding	53,423,575	53,190,790
Dilutive effect of outstanding stock options, warrants and restricted stock grants (as determined by the application of the treasury stock method)	11,109,142	12,066,413
Dilutive effect of Series A debentures	-	858,443
Dilutive effect of 8-1/2% convertible trust originated preferred securities	10,332,920	10,332,920
Dilutive effect of 6-3/4% convertible subordinated notes	7,617,155	5,245,514
Weighted average number of common shares out-		

standing, as adjusted. 82,482,792 81,694,080

(continued on next page)

Exhibit 11.1
Page 4 of 6

CONTINENTAL AIRLINES, INC.
STATEMENT REGARDING COMPUTATION OF PER SHARE EARNINGS (1) (2)
(In thousands of dollars, except per share data)

	Three Months Ended September 30, 1996	Nine Months Ended September 30, 1996
Income before extraordinary loss applicable to common shares.	\$ 22,704	\$ 275,530
Add interest expense associated with the assumed reduction of borrowings, net of federal income tax effect	-	-
Add interest expense associated with the assumed conversion of convertible debentures	-	440
Add interest expense associated with the assumed conversion of 8-1/2% convertible trust originated preferred securities, net of federal income tax effect	3,203	11,651
Add interest expense associated with the assumed conversion of 6-3/4% convertible subordinated notes, net of federal income tax effect.	2,342	4,912
Income before extraordinary loss, as adjusted.	\$ 28,249	\$ 292,533
Per share amount.	\$ 0.34	\$ 3.58

(1) On June 26, 1996, the Board of Directors of the Company declared a two-for-one stock split (the "Stock Split") pursuant to which (a) one share of the Company's Class A common stock, par value \$.01 per share, was

issued for each share of Class A common stock outstanding on July 2, 1996 (the "Record Date") and (b) one share of the Company's Class B common stock, par value \$.01 per share, was issued for each share of Class B common stock outstanding on the Record Date. Shares issuable pursuant to the Stock Split were distributed on or about July 16, 1996. All share and earnings per share information for prior periods has been adjusted for the Stock Split.

(2) Excludes extraordinary net loss on early extinguishment of debt of \$6.3 million.

Exhibit 11.1
Page 5 of 6

CONTINENTAL AIRLINES, INC.
STATEMENT REGARDING COMPUTATION OF PER SHARE EARNINGS (1)
(In thousands of dollars, except per share data)

	Three Months		Nine Months	
	Ended September 30,		Ended September 30,	
	1996	1995	1996	1995
Fully diluted:				
Weighted average shares outstanding	53,423,575	52,101,304	53,190,790	51,555,420
Dilutive effect of outstanding stock options, warrants and restricted stock grants (as determined by the application of the treasury stock method)	11,109,142	18,631,626	12,066,413	12,917,706
Dilutive effect of Series A debentures	-	11,206,692	858,443	3,776,614
Dilutive effect of 8-1/2% convertible trust originated preferred securities	-	-	10,332,920	-
Dilutive effect of 6-3/4% convertible subordinated notes	-	-	5,245,514	-
Weighted average number of common shares outstanding, as adjusted	64,532,717	81,939,622	81,694,080	68,249,740

(continued on next page)

Exhibit 11.1
Page 6 of 6

CONTINENTAL AIRLINES, INC.
STATEMENT REGARDING COMPUTATION OF PER SHARE EARNINGS (1)

(In thousands of dollars, except per share data)

	Three Months		Nine Months	
	Ended September 30,		Ended September 30,	
	1996	1995	1996	1995
Income applicable to common shares	\$ 16,424	\$ 105,876	\$ 269,250	\$ 174,642
Add interest expense associated with the assumed reduction of borrowings, net of federal income tax effect	-	2,067	-	6,093
Add interest expense associated with the assumed conversion of convertible debentures .	-	1,849	440	1,849
Add interest expense associated with the assumed conversion of 8-1/2% convertible trust originated preferred securities, net of federal income tax effect	-	-	11,651	-
Add interest expense associated with the assumed conversion of 6-3/4% convertible subordinated notes, net of federal income tax effect	-	-	4,912	-
Income, as adjusted	\$ 16,424	\$ 109,792	\$ 286,253	\$ 182,584
Per share amount	\$ 0.25	\$ 1.34	\$ 3.50	\$ 2.68

(1) On June 26, 1996, the Board of Directors of the Company declared a two-for-one stock split (the "Stock Split") pursuant to which (a) one share of the Company's Class A common stock, par value \$.01 per share, was issued for each share of Class A common stock outstanding on July 2, 1996 (the "Record Date") and (b) one share of the Company's Class B common stock, par value \$.01 per share, was issued for each share of Class B common stock outstanding on the Record Date. Shares issuable pursuant to the Stock Split were distributed on or about July 16, 1996. All share and earnings per share information for prior periods has been adjusted for the Stock Split.

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Risk Factors Relating to the Company

Continental's History of Operating Losses

Although Continental recorded net income of \$224 million in 1995 and \$272 million in the nine months ended September 30, 1996, it had experienced significant operating losses in the previous eight years. In the long term, Continental's viability depends on its ability to sustain profitable results of operations.

Leverage and Liquidity

Continental has successfully negotiated a variety of agreements to increase its liquidity during 1995 and 1996. Nevertheless, Continental remains more leveraged and has significantly less liquidity than certain of its competitors, several of whom have available lines of credit and/or significant unencumbered assets. Accordingly, Continental may be less able than certain of its competitors to withstand a prolonged recession in the airline industry.

As of September 30, 1996, Continental and its consolidated subsidiaries had approximately \$1.7 billion (including current maturities) of long-term indebtedness and capital lease obligations and had approximately \$870 million of minority interest, Continental-obligated mandatorily redeemable preferred securities of subsidiary trust, redeemable warrants, redeemable preferred stock and common stockholders' equity. Common stockholders' equity reflects the adjustment of the Company's balance sheet and the recording of assets and liabilities at fair market value as of April 27, 1993 in accordance with fresh start reporting.

During the first and second quarters of 1995, in connection with negotiations with various lenders and lessors, Continental ceased or reduced contractually required payments under various agreements, which produced a significant number of events of default under debt, capital lease and operating lease agreements. Through agreements reached with the various lenders and lessors, Continental has cured all of these events of default. The last such agreement was put in place during the fourth quarter of 1995.

As of September 30, 1996, Continental had approximately \$865 million of cash and cash equivalents, including restricted cash and cash equivalents of \$70 million. Continental does not have general lines of credit and has significant encumbered assets.

Continental had firm commitments with The Boeing Company ("Boeing") to take delivery of 43 new jet aircraft during the years 1997 through 2002. During the third quarter of 1996, Continental amended the terms of its commitments with Boeing to take delivery of a total of 61 jet aircraft during the years 1997 through 2003 with options for an additional 23 aircraft. These amendments changed the aircraft mix and timing of delivery of aircraft, in order to more closely match Continental's anticipated future aircraft needs. In addition, in October 1996, Continental placed an order for 60 firm 737-500 and 737-600 aircraft that will replace older, less efficient Stage 2 aircraft between August 1997 and December 1999. The estimated aggregate cost of the Company's firm commitment Boeing aircraft is in excess of \$4 billion. The Company has commitments of approximately \$1.4 billion of backstop financing for its Boeing aircraft orders. Continental currently plans to finance the indebtedness on its new aircraft using enhanced equipment trust certificates or similar financing, subject to availability and market conditions. However, further financing will be needed to satisfy the Company's capital commitments for new Boeing aircraft. There can be no assurance that sufficient financing will be available for all aircraft and other capital expenditures not covered by firm financing commitments. The Company has also entered into agreements with several outside parties to lease four DC-10-30 aircraft and to purchase three DC-10-30 aircraft and two MD-82 aircraft. These nine aircraft are

expected to be delivered during the period from October 1996 through mid-year 1997, and the Company expects to finance the aircraft to be purchased from available cash or from third party sources.

In addition, in March 1996, Continental's wholly owned subsidiary, Continental Express, Inc. ("Express"), entered into an agreement to acquire eight new ATR aircraft. As of September 1996, five of these aircraft had been delivered. The aircraft are being accounted for as operating leases. In conjunction with the acquisition, the Company is returning eight older ATR aircraft accounted for as capital leases. As of September 1996, four of these aircraft had been returned. Also, in September 1996, Express announced an order for 25 firm EMB-145 50-seat regional jets with options for an additional 175 aircraft. Express plans to account for these aircraft as operating leases. Neither Express nor Continental will have any obligation to take aircraft which are not financed by a third party and leased to Express. Continental will guarantee Express' obligations under the operating leases. Express will take delivery of the 25 firm aircraft during the period from December 1996 through the third quarter of 1998.

For 1996, Continental expects to incur cash expenditures under operating leases relating to aircraft of approximately \$568 million, compared with \$521 million for 1995, and approximately \$229 million relating to facilities and other rentals, the same amount as for 1995. In addition, Continental has capital requirements relating to compliance with regulations that are discussed below. See "Regulatory Matters."

In July 1996, Continental's 91%-owned subsidiary, Continental Micronesia, Inc. ("CMI"), consummated a \$320 million secured term loan financing with a group of banks and other financial institutions. The loan was made in two tranches -- a \$180 million five-year amortizing term loan with a floating interest rate of LIBOR plus 175 basis points and a \$140 million seven-year amortization extended loan with a floating interest rate of LIBOR plus 200 basis points. The loan is secured by the stock of CMI and substantially all its unencumbered assets, consisting primarily of CMI's route authorities, and is guaranteed by Continental and Air Micronesia, Inc. ("AMI") (CMI's parent company).

CMI used the net proceeds of the financing to prepay \$160 million in principal amount of indebtedness to an affiliate of General Electric Company (General Electric Company and affiliates, collectively "GE") and to pay transaction costs, and Continental used the \$136 million in proceeds received by it as an indirect dividend from CMI, together with approximately \$28 million in cash on hand, to prepay approximately \$164 million in principal amount of indebtedness to GE. The bank financing does not contain any restrictive covenants at the Continental parent level, and none of the assets of Continental Airlines, Inc. (other than its stock in AMI) is pledged in connection with the new financing.

The bank financing contains significant financial covenants relating to CMI, including maintenance of a minimum fixed charge coverage ratio, a minimum consolidated net worth and minimum liquidity, and covenants restricting CMI's leverage, its incurrence of certain indebtedness and its pledge of assets. The financial covenants also limit the ability of CMI to pay dividends to Continental.

In July 1996, the Company announced its plan to expand its gates and related facilities in Terminal B, as well as planned improvements at Terminal C, at Continental's Houston Intercontinental Airport hub. The expansion is expected to cost approximately \$115 million, which the Company expects will be funded principally by the issuance of tax-exempt debt by the applicable municipal authority. In connection therewith, the Company expects to enter into long-term leases (or amendments to existing leases) with the applicable municipal authority containing rental payments sufficient to service the related tax-exempt debt.

Aircraft Fuel

Since fuel costs constitute a significant portion of Continental's operating costs (approximately 12.5% for the year ended December 31, 1995 and 12.8% for the nine months ended September 30, 1996), significant changes in fuel costs would materially affect the Company's operating results. Jet fuel prices have recently increased. Fuel prices continue to be susceptible to international events, and the Company cannot predict near or longer-term fuel prices. The Company has entered into petroleum option contracts to provide some short-term protection (currently approximately six months) against a sharp increase in jet fuel prices. In the event of a fuel supply shortage resulting from a disruption of oil imports or otherwise, higher fuel prices or curtailment of scheduled service could result.

Certain Tax Matters

The Company's United States federal income tax return reflects net operating loss carryforwards ("NOLs") of \$2.6 billion, subject to audit by the Internal Revenue Service, of which \$1.3 billion are not subject to the limitations of Section 382 of the Internal Revenue Code ("Section 382"). As a result, the Company will not pay United States federal income taxes (other than alternative minimum tax) until it has recorded approximately an additional \$1.3 billion of taxable income following December 31, 1995. For financial reporting purposes, Continental began accruing tax expense on its income statement during the second quarter of 1996. Section 382 imposes limitations on a corporation's ability to utilize NOLs if it experiences an "ownership change." In general terms, an ownership change may result from transactions increasing the ownership of certain stockholders in the stock of a corporation by more than 50 percentage points over a three-year period. The sale of the Company's common stock in its secondary offering gave rise to an increase in percentage ownership by certain stockholders for this purpose. Based upon the advice of its counsel, Cleary, Gottlieb, Steen & Hamilton, the Company believes that such percentage increase did not give rise to an ownership change under Section 382. However, no assurance can be given that future transactions, whether within or outside the control of the Company, will not cause a change in ownership, thereby substantially limiting the potential utilization of the NOLs in a given future year. In the event that an ownership change should occur, utilization of Continental's NOLs would be subject to an annual limitation under Section 382 determined by multiplying the value of the Company's stock (including both common and preferred stock) at the time of the ownership change by the applicable long-term tax exempt rate (which was 5.63% for September 1996). Unused annual limitations may be carried over to later years, and the amount of the limitation may under certain circumstances be increased by the built-in gains in assets held by the Company at the time of the change that are recognized in the five-year period after the change. Under current conditions, if an ownership change were to occur, Continental's NOL utilization would be limited to approximately \$100 million per year.

In connection with the Company's 1993 reorganization under Chapter 11 of the U.S. bankruptcy code effective April 27, 1993 (the "Reorganization") and the recording of assets and liabilities at fair market value under the American Institute of Certified Public Accountants' Statement of Position 90-7 - "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code" ("SOP 90-7"), the Company recorded a deferred tax liability at April 27, 1993, net of the amount of the Company's estimated realizable NOLs as required by Statement of Financial Accounting Standards No. 109 - "Accounting for Income Taxes." Realization of a substantial portion of the Company's NOLs will require the completion during the five-year period following the Reorganization of transactions resulting in recognition of built-in gains for federal income tax purposes. The Company has consummated one such transaction, which had the effect of realizing approximately 40% of the built-in gains required to be realized over the five-year period, and currently intends to consummate one or more additional transactions. If the Company were to determine in the future that not all such transactions will be completed, an adjustment to the net deferred tax liability of up to \$116 million would be charged to income in the period such determination was made.

CMI

CMI's operating profit margins have consistently been greater than the Company's margins overall. In addition to its non-stop service between Honolulu and Tokyo, CMI's operations focus on the neighboring islands of Guam and Saipan, resort destinations that cater primarily to Japanese travelers. Because the majority of CMI's traffic originates in Japan, its results of operations are substantially affected by the Japanese economy and changes in the value of the yen as compared to the dollar. Appreciation of the yen against the dollar during 1993 and 1994 increased CMI's profitability and a decline of the yen against the dollar may be expected to decrease it. The yen has declined against the dollar during 1996 as compared to 1995. To reduce the potential negative impact on CMI's dollar earnings, CMI, from time to time, purchases average rate options as a hedge against a portion of its expected net yen cash flow position. Any significant and sustained decrease in traffic or yields to and from Japan could materially adversely affect Continental's consolidated profitability.

Principal Stockholders

As of September 30, 1996, Air Canada held approximately 10.0% of the common equity interests and 4.0% of the general voting power of the Company, and Air Partners, L.P. ("Air Partners") held approximately 9.8% of the common equity interests and 39.3% of the general voting power of the Company. In addition, assuming exercise of all of the warrants held by Air Partners, approximately 23.2% of the common equity interests and 52.0% of the general voting power would be held by Air Partners. Air Canada has announced its intention to divest its interest in the Company during December 1996 or early 1997, subject to market conditions. At any time after January 1, 1997, shares of Class A common stock may be freely converted into an equal number of shares of Class B common stock. Such conversion would effectively increase the relative voting power of those Class A stockholders who do not convert.

Various provisions in the Company's Amended and Restated Certificate of Incorporation (the "Certificate of Incorporation") and Bylaws (the "Bylaws") currently provide Air Partners with the right to elect one-third of the directors in certain circumstances; these provisions could have the effect of delaying, deferring or preventing a change in control of the Company.

Risk Factors Relating to the Airline Industry

Industry Conditions and Competition

The airline industry is highly competitive and susceptible to price discounting. The Company has in the past both responded to discounting actions taken by other carriers and initiated significant discounting actions itself. Continental's competitors include carriers with substantially greater financial resources, as well as smaller carriers with lower cost structures. Airline profit levels are highly sensitive to, and during recent years have been severely impacted by, changes in fuel costs, fare levels (or "average yield") and passenger demand. Passenger demand and yields have been adversely affected by, among other things, the general state of the economy, international events and actions taken by carriers with respect to fares. From 1990 to 1993, these factors contributed to the domestic airline industry's incurring unprecedented losses. Although fare levels have increased recently, significant industry-wide discounts could be reimplemented at any time, and the introduction of broadly available, deeply discounted fares by a major United States airline would likely result in lower yields for the entire industry and could have a material adverse effect on the Company's operating results.

The airline industry has consolidated in past years as a result of mergers and liquidations and may further consolidate in the future. Among other effects, such consolidation has allowed certain of Continental's major competitors to expand (in particular) their

international operations and increase their market strength. Furthermore, the emergence in recent years of several new carriers, typically with low cost structures, has further increased the competitive pressures on the major United States airlines. In many cases, the new entrants have initiated or triggered price discounting. Aircraft, skilled labor and gates at most airports continue to be readily available to start-up carriers. Although management believes that Continental is better able than some of its major competitors to compete with fares offered by start-up carriers because of its lower cost structure, competition with new carriers or other low cost competitors on Continental's routes could negatively impact Continental's operating results.

Regulatory Matters

In the last several years, the United States Federal Aviation Administration (the "FAA") has issued a number of maintenance directives and other regulations relating to, among other things, retirement of older aircraft, collision avoidance systems, airborne windshear avoidance systems, noise abatement, commuter aircraft safety and increased inspections and maintenance procedures to be conducted on older aircraft. The Company expects to continue incurring expenses for the purpose of complying with the FAA's noise and aging aircraft regulations. In addition, several airports have recently sought to increase substantially the rates charged to airlines, and the ability of airlines to contest such increases has been restricted by federal legislation, U.S. Department of Transportation regulations and judicial decisions.

Management believes that the Company benefitted significantly from the expiration of the aviation trust fund tax (the "ticket tax") on December 31, 1995, although the amount of any such benefit directly resulting from the expiration of the ticket tax cannot precisely be determined. The ticket tax was reimposed on August 27, 1996, and is again scheduled to expire on December 31, 1996. Management believes that the reimposition of the ticket tax has a negative impact on the Company, although the amount of such negative impact directly resulting from the reimposition of the ticket tax cannot be precisely determined.

Additional laws and regulations have been proposed from time to time that could significantly increase the cost of airline operations by imposing additional requirements or restrictions on operations. Laws and regulations have also been considered that would prohibit or restrict the ownership and/or transfer of airline routes or takeoff and landing slots. Also, the availability of international routes to United States carriers is regulated by treaties and related agreements between the United States and foreign governments that are amendable. Continental cannot predict what laws and regulations may be adopted or their impact, but there can be no assurance that laws or regulations currently proposed or enacted in the future will not adversely affect the Company.

Replacement Decision Expected
to have Positive Future Results*

(\$Millions)	-----Estimated-----					
	1996	1997	1998	1999	2000	2001
Aircraft Ownership	-	6	(56)	(116)	(121)	(125)
Maintenance/Inventory	-	30	78	135	153	157
Fuel	-	1	20	49	67	69
Pilots/Training	-	(9)	(11)	(2)	16	15
Other	(128)	-	-	-	-	-
Total Pre-Tax	(128)	28	31	66	115	116

*See information concerning forward looking statements under Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and see Assumptions in Appendix A, below.

Appendix A - Assumptions

Aircraft Ownership

All new aircraft leased assuming a lease factor of .80% per month.

All old aircraft are assumed to continue as leased or owned with leases on leased aircraft being renewed at market rates and the cost of hushkits and upgraded interiors being 100% financed by Continental at 9.5% and depreciated over 10 to 15 years depending on fleet type.

Aircraft ownership compares the ownership costs of new aircraft versus old aircraft had they been refurbished with hushkits and upgraded interiors. In addition, new aircraft provide a utilization benefit because there is less time allocated for planned and unplanned maintenance. Initial pilot training is capitalized for the new 737-600/800 fleet types. As a result of the write-down of owned aircraft, depreciation related to the owned aircraft was reduced.

Maintenance/Inventory

Maintenance expense savings are determined based on the difference between the planned hangar schedule for new versus old aircraft (comparison by fleet type by maintenance event at budgeted cost per event). Maintenance overhead expense is reduced by \$15 million per year based on eliminating fleet-specific expenses for the three retired fleet types.

As a result of the inventory write-down to net realizable value, future depreciation of related inventory will be reduced.

Fuel Expense - Fuel expense savings are calculated based on the planned block hour fuel burn rates for new versus old aircraft, using a base price per gallon of \$.575 (1996 dollars).

Pilot/Training

Pilot expense savings will result as 3-pilot 727s are replaced with 2-pilot 737-800s.

737-500 initial pilot training and all "cascade" training that will result as new replacement aircraft enter service are expensed when incurred. Expense is calculated by forecasting the number of training cycles required at an average cost per training cycle versus training cycles required had stage II aircraft remained.

Annual pilot training expense will be reduced on average by \$2

million as the number of fleet types decreases (less cascade training required with fewer fleet types).

Other - Other costs in 1996 consist of a non-recurring charge due to the write-down of inventory and other expenses related to the stage II aircraft being retired.

General - Inflation is assumed to be three percent per year during this time period.