2023

Management’s Discussion and Analysis of Results of Operations and Financial Condition

February 16, 2024

AIR CANADA

A STAR ALLIANCE MEMBER

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1. SELECTED FINANCIAL METRICS AND STATISTICS

The financial and operating highlights for Air Canada for the periods indicated are as follows:

(Canadian dollars in millions, except per share data or where indicated)	Fourth Quarter			Full Year		
Financial Performance Metrics	**2023**	**2022**	**$ Change**	**2023**	**2022**	**$ Change**
Operating revenues	5,175	4,680	495	21,833	16,556	5,277
Operating income (loss)	79	(28)	107	2,279	(187)	2,466
Operating margin (1) (%)	1.5	(0.6)	2.1 pp (8)	10.4	(1.1)	11.5 pp
Adjusted EBITDA (2)	521	389	132	3,982	1,457	2,525
Adjusted EBITDA margin (2) (%)	10.1	8.3	1.8 pp	18.2	8.8	9.4 pp
Income (loss) before income taxes	122	146	(24)	2,212	(1,524)	3,736
Net income (loss)	184	168	16	2,276	(1,700)	3,976
Adjusted pre-tax income (loss) (2)	(47)	(211)	164	1,693	(952)	2,645
Adjusted net income (loss) (2)	(44)	(217)	173	1,713	(988)	2,701
Total liquidity (3)	10,290	9,824	466	10,290	9,824	466
Net cash flows from operating activities	985	647	338	4,320	2,368	1,952
Free cash flow (2)	669	320	349	2,756	796	1,960
Net debt (2)	4,567	7,495	(2,928)	4,567	7,495	(2,928)
Diluted earnings (loss) per share	0.41	0.41	-	5.96	(4.75)	10.71
Adjusted earnings (loss) per share (2)	(0.12)	(0.61)	0.49	4.56	(2.76)	7.32
Operating Statistics (4)	**2023**	**2022**	**Change %**	**2023**	**2022**	**Change %**
Revenue passenger miles (RPMs) (millions)	20,405	18,525	10.1	85,802	66,495	29.0
Available seat miles (ASMs) (millions)	24,439	22,368	9.3	99,012	82,558	19.9
Passenger load factor %	83.5%	82.8%	0.7 pp	86.7%	80.5%	6.1 pp
Passenger revenue per RPM (Yield) (cents)	22.3	21.9	1.8	22.6	21.4	6.0
Passenger revenue per ASM (PRASM) (cents)	18.6	18.2	2.6	19.6	17.2	13.6
Operating revenue per ASM (cents)	21.2	20.9	1.2	22.1	20.1	10.0
Operating expense per ASM (CASM) (cents)	20.9	21.1	(0.9)	19.8	20.3	(2.6)
Adjusted CASM (cents) (2)	14.2	13.7	4.1	13.5	13.2	2.2
Average number of full-time-equivalent (FTE) employees (thousands) (5)	36.4	33.2	9.7	35.7	30.5	17.1
Aircraft in operating fleet at period-end	361	345	5	361	345	5
Seats dispatched (thousands)	13,636	12,690	7.4	54,026	47,038	14.9
Aircraft frequencies (thousands)	93.4	89.9	3.9	373.1	340.5	9.6
Average stage length (miles) (6)	1,792	1,763	1.7	1,833	1,755	4.4
Fuel cost per litre (cents)	117.6	134.3	(12.4)	111.6	130.1	(14.2)
Fuel litres (thousands)	1,178,926	1,084,569	8.7	4,751,692	4,056,788	17.1
Revenue passengers carried (thousands) (7)	10,899	10,098	7.9	44,790	36,144	23.9

(1) Operating margin is a supplementary financial measure and is defined as operating income (loss) as a percentage of operating revenues.

(2) Adjusted EBITDA (earnings before interest, taxes, depreciation, and amortization), adjusted EBITDA margin, adjusted pre-tax income (loss), adjusted net income (loss), free cash flow, net debt, adjusted earnings (loss) per share, and adjusted CASM are non-GAAP financial measures, capital management measures, non-GAAP ratios or supplementary financial measures. Such measures are not recognized measures for financial statement presentation under GAAP, do not have standardized meanings, may not be comparable to similar measures presented by other entities and should not be considered a substitute for or superior to GAAP results. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for descriptions of Air Canada's non-GAAP financial measures and for a quantitative reconciliation of Air Canada's non-GAAP financial measures to the most comparable GAAP measure.

(3) Total liquidity refers to the sum of cash, cash equivalents, short and long-term investments, and the amounts available under Air Canada's credit facilities. Total liquidity, as at December 31, 2023, of $10,290 million consisted of $9,295 million in cash, cash equivalents, short and long-term investments and $995 million available under undrawn credit facilities. As at December 31, 2022, total liquidity of $9,824 million consisted of $8,811 million in cash and cash equivalents, short and long-term investments, and $1,013 million available under undrawn credit facilities. These amounts also include funds ($393 million as at December 31, 2023 and $386 million as at December 31, 2022) held in trust by Air Canada Vacations in accordance with regulatory requirements governing advance sales for tour operators.

(4) Except for the reference to average number of FTE employees, operating statistics in this table include third party carriers operating under capacity purchase agreements with Air Canada.

(5) Reflects FTE employees at Air Canada and its subsidiaries. Excludes FTE employees at third party carriers operating under capacity purchase agreements with Air Canada.

(6) Average stage length is calculated by dividing the total number of available seat miles by the total number of seats dispatched.

(7) Revenue passengers are counted on a flight number basis (rather than by journey/itinerary or by leg) which is consistent with the IATA definition of revenue passengers carried.

(8) "pp" denotes percentage points and refers to a measure of the arithmetic difference between two percentages.

2. INTRODUCTION AND KEY ASSUMPTIONS

In this Management's Discussion and Analysis of Results of Operations and Financial Condition ("MD&A"), the Corporation refers, as the context may require, to Air Canada and/or one or more of Air Canada's subsidiaries, including its wholly owned operating subsidiaries, Aeroplan Inc. (Aeroplan), Touram Limited Partnership, doing business under the brand name Air Canada Vacations® (Air Canada Vacations), and Air Canada Rouge LP, doing business under the brand name Air Canada Rouge® (Air Canada Rouge). This MD&A provides the reader with a review and analysis, from the perspective of management, of Air Canada's financial results for the fourth quarter and full year 2023. This MD&A should be read in conjunction with Air Canada's 2023 annual audited consolidated financial statements and notes dated February 16, 2024. All financial information has been prepared in accordance with generally accepted accounting principles in Canada (GAAP), as set out in the CPA Canada Handbook – Accounting (CPA Handbook), which incorporates International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IFRS Accounting Standards), except for any non-GAAP measures and any financial information specifically denoted otherwise.

Except as otherwise noted, monetary amounts are stated in Canadian dollars. For an explanation of certain terms used in this MD&A, refer to section 21 "Glossary" of this MD&A. Except as otherwise noted or where the context may otherwise require, this MD&A is current as of February 15, 2024.

Forward-looking statements are included in this MD&A. See "Caution Regarding Forward-Looking Information" below for a discussion of risks, uncertainties and assumptions relating to these statements. For a description of risks relating to Air Canada, refer to section 18 "Risk Factors" of this MD&A. Air Canada issued a news release dated February 16, 2024 reporting on its results for the fourth quarter and full year 2023. This news release is available on Air Canada's website at **aircanada.com** and on SEDAR+ website at **www.sedarplus.com**. For further information on Air Canada's public disclosures, including Air Canada's Annual Information Form, consult SEDAR+ at **www.sedarplus.com**.

Caution Regarding Forward-Looking Information

Air Canada's public communications may include forward-looking statements within the meaning of applicable securities laws. Forward-looking statements relate to analyses and other information that are based on forecasts of future results and estimates of amounts not yet determinable. These statements may involve, but are not limited to, comments relating to guidance, strategies, expectations, planned operations or future actions. Forward-looking statements are identified using terms and phrases such as "preliminary", "anticipate", "believe", "could", "estimate", "expect", "intend", "may", "plan", "predict", "project", "will", "would", and similar terms and phrases, including references to assumptions.

Forward-looking statements, by their nature, are based on assumptions including those described herein and are subject to important risks and uncertainties. Forward-looking statements cannot be relied upon due to, among other things, changing external events and general uncertainties of the business of Air Canada. Actual results may differ materially from results indicated in forward-looking statements due to a number of factors, including those discussed below.

Factors that may cause results to differ materially from results indicated in forward-looking statements include economic conditions as well as geopolitical conditions such as the military conflicts in the Middle East and between Russia and Ukraine, Air Canada's ability to successfully achieve or sustain positive net profitability, industry and market conditions and the demand environment, competition, Air Canada's dependence on technology, cybersecurity risks, interruptions of service, climate change and environmental factors (including weather systems and other natural phenomena and factors arising from anthropogenic sources), Air Canada's dependence on key suppliers (including government agencies and other stakeholders supporting airport and airline operations), employee and labour relations and costs, Air Canada's ability to successfully implement appropriate strategic and other important initiatives (including Air Canada's ability to manage operating costs), energy prices, Air Canada's ability to pay its indebtedness and maintain or increase liquidity, Air Canada's dependence on regional and other carriers, Air Canada's ability to attract and retain required personnel, epidemic diseases, changes in laws, regulatory developments or proceedings, terrorist acts, war, Air Canada's ability to successfully operate its loyalty program, casualty losses, Air Canada's dependence on Star Alliance® and joint ventures, Air Canada's ability to preserve and grow its brand, pending and future litigation and actions by third parties, currency exchange fluctuations, limitations due to restrictive covenants, insurance issues and costs, and pension plan obligations as well as the factors identified in Air Canada's public disclosure file available at www.sedarplus.com and, in particular, those identified in section 18 "Risk Factors" of this MD&A.

Air Canada has and continues to establish targets, make commitments and assess the impact regarding climate change, and related initiatives, plans and proposals that Air Canada and other stakeholders (including government, regulatory and other bodies) are pursuing in relation to climate change and carbon emissions. The achievement of our commitments and targets depends on many factors, including the combined actions of governments, industry, suppliers and other stakeholders and actors, as well as the development and implementation of new technologies. In particular, our 2030 and 2050 carbon emission related targets are ambitious, and heavily dependent on new technologies, renewable energies and the availability of sufficient a supply of sustainable aviation fuels (SAF) which continues to present serious challenges. In addition, Air Canada has incurred, and expects to continue to incur, costs to achieve its goal of net-zero carbon emissions and to comply with environmental sustainability legislation and regulation and other standards and accords. The precise nature of future binding or non-binding legislation, regulation, standards and accords, on which local and international stakeholders are increasingly focusing, cannot be predicted with any degree of certainty, nor can their financial, operational or other impact. There can be no assurance of the extent to which any of our climate goals will be achieved or that any future investments that we make in furtherance of achieving our climate goals will produce the expected results or meet increasing stakeholder environmental, social and governance expectations. Moreover, future events could lead Air Canada to prioritize other nearer-term interests over progressing toward our current climate goals based on business strategy, economic, regulatory and social factors, and potential pressure from investors, activist groups or other stakeholders. If we are unable to meet or properly report on our progress toward achieving our climate change goals and commitments, we could face adverse publicity and reactions from investors, customers, advocacy groups or other stakeholders, which could result in reputational harm or other adverse effects to Air Canada. The forward-looking statements contained or incorporated by reference in this MD&A represent Air Canada's expectations as of the date of this MD&A (or as of the date they are otherwise stated to be made) and are subject to change after such date. However, Air Canada disclaims any intention or obligation to update or revise any forward-looking statements, whether because of new information, future events or otherwise, except as required under applicable securities regulations.

Key Assumptions

Assumptions were made by Air Canada in preparing and making forward-looking statements. As part of its assumptions, Air Canada assumes moderate Canadian GDP growth for 2024. Air Canada also assumes that the Canadian dollar will trade, on average, at C$1.33 per U.S. dollar for the full year 2024 and that the price of jet fuel will average C$1.00 per litre for the full year 2024.

Intellectual Property

Air Canada owns or has rights to trademarks, service marks or trade names used in connection with the operation of its business. In addition, Air Canada's names, logos and website names and addresses are owned or licensed by Air Canada. Air Canada also owns or has the rights to copyrights that also protect the content of its products and/or services. Solely for convenience, the trademarks, service marks, trade names and copyrights referred to in this MD&A may be listed without the ©, ® and ™ symbols, but Air Canada reserves all rights to assert, to the fullest extent under applicable law, its rights, or the rights of the applicable licensors to these trademarks, service marks, trade names and copyrights. This MD&A may also include trademarks, service marks or trade names of other parties. Air Canada's use or display of other parties' trademarks, service marks, trade names or products is not intended to, and does not imply a relationship with, or endorsement or sponsorship of Air Canada by, the trademark, service mark or trade name owners or licensees.

Incorporation of Other Information

No information contained on or accessed via Air Canada's websites (or any other website referred to in this MD&A), and no document referred to in this MD&A, is incorporated into or forms part of this MD&A, except if it is expressly stated in this MD&A to be incorporated into this MD&A.

3. ABOUT AIR CANADA

Air Canada is the largest provider of scheduled passenger services in the Canadian market, the Canada-U.S. transborder market, and in the international market to and from Canada. Its mission is connecting Canada and the world.

Air Canada enhances its domestic and transborder network through commercial agreements with regional carriers, including a capacity purchase agreement (CPA) with Jazz Aviation LP (Jazz), a wholly owned subsidiary of Chorus Aviation Inc., operating flights on behalf of Air Canada under the Air Canada Express brand. Regional flying forms an integral part of the airline's international network strategy, providing valuable traffic feed to Air Canada and Air Canada Rouge routes.

Air Canada is a founding member of the Star Alliance® network. Through the 26-member airline network, Air Canada offers its customers access to a wide global network, as well as reciprocal participation in frequent flyer programs, a seamless travel experience and improved customer service, including the use of airport lounges and other common airport facilities.

Air Canada's Aeroplan program is Canada's premier travel loyalty program. The Aeroplan program allows individuals to enrol as members and accumulate Aeroplan points through travel on Air Canada and select partners, as well as through the purchase of products and services from participating partners and suppliers. Members can redeem Aeroplan points for a variety of travel, merchandise, gift cards and other rewards provided directly by participating partners or made available through Aeroplan's suppliers. Aeroplan Elite Status recognizes Air Canada's frequent flyers, as well as Aeroplan's most engaged members, with a range of priority travel services and membership benefits.

Air Canada Cargo, a division of Air Canada, is a global cargo service provider, offering cargo services on passenger flights and on dedicated Boeing 767 freighter aircraft.

Air Canada Vacations is a leading Canadian tour operator, developing, marketing and distributing vacation travel packages in the outbound leisure travel market (Caribbean, Mexico, U.S., Europe, Central and South America, South Pacific, Australia and Asia) and the inbound leisure travel market to destinations within Canada, and offering cruise packages in North America, Europe and the Caribbean. Air Canada Rouge is Air Canada's leisure carrier.

4. OVERVIEW

The year 2023 was pivotal for Air Canada. Having stabilized and recovered from the COVID-19 pandemic, Air Canada achieved sound financial results while significantly progressing on its strategic priorities. Air Canada's full year financial results and operational performance improved from 2022, despite the challenges and uncertainties posed by geopolitical events, inflationary pressures and supply chain issues affecting the aerospace industry. While COVID-19-related travel restrictions and health measures were still present in 2022, in Canada, most of the remaining restrictions were eased leading into the summer of 2022 and, effective October 1, 2022, all remaining Government of Canada restrictions were lifted.

During 2023, Air Canada continued to invest in new products and services, strengthen its various partnerships and advance its innovation agenda. The main drivers for the year over year improvements in its financial and operating results included:

- 20% year-over-year increase in operated capacity.
- 188 direct destinations compared to 185 destinations in 2022.
- 1,025 average daily flights, compared to 945 average daily flights in 2022.
- Year-over-year increase in yields driven by a strong pricing environment.
- Strong demand for premium products in all markets.
- Strengthened partnerships and collaborations.

Corporate Strategy

Air Canada's vision is predicated on leveraging the solid foundation it has built over the past several years to restore and rebuild toward its global champion ambition, while taking advantage of groundbreaking opportunities and continuing to execute on Air Canada's unwavering commitment to safety, service excellence and the customer journey.

Air Canada is evolving its business for the future. "Rise Higher," Air Canada's business imperatives framework supporting its corporate strategy, is intended to elevate everything about its business. In pursuing its Rise Higher principles, Air Canada is working to:

- Fund its future by staying vigilant on costs, seizing on opportunities and making the right strategic investments.
- Reach new frontiers by embracing its competitive strengths to grow its business, expanding its international reach and exploring new opportunities.
- Elevate its customers by supporting the creation of meaningful customer experiences and human connections, such as by leveraging innovations in technology, loyalty program and products.
- Foster a collaborative workplace that respects all diverse cultures and contributions to society.

2023 Highlights

Funding the future

Air Canada prepaid about $1.3 billion of outstanding debt, including financing on 33 Airbus A220 and five Boeing 787-8 aircraft. As a result of prepayments, these aircraft have been added to Air Canada's unencumbered asset pool, bringing the total estimated value to approximately $6.6 billion at December 31, 2023, excluding the value of Aeroplan. At December

31, 2023, Air Canada's leverage ratio was 1.1, a significant improvement from a leverage ratio of 5.1 at December 31, 2022.

Air Canada added 12 aircraft to its operating fleet, which consisted of six wide-body aircraft, including two Boeing 767 freighters, and six narrow-body aircraft. In 2023, Air Canada also entered into agreements to acquire 18 Boeing 787-10 aircraft with options for an additional 12 aircraft. Deliveries are expected to begin in the fourth quarter of 2025 with the last delivery scheduled for the first quarter of 2027.

Reaching New Frontiers

Air Canada continued to restore its North American and international network, resulting in a 20% increase in operated capacity from 2022.

In the domestic market, Air Canada resumed several seasonal routes, increased frequencies on certain domestic routes and launched non-stop services between Montréal and Fort McMurray, and between Toronto and Yellowknife. In the transborder market, Air Canada launched routes between Toronto and Montréal to New York JFK airport and between Toronto and Sacramento, restored 13 transborder routes and increased frequency on over a dozen U.S. routes. For international markets, Air Canada added new transatlantic services to Brussels, Amsterdam, Toulouse, Copenhagen and Dubai. It also resumed key Asia services to Tokyo-Haneda and Osaka, increased frequencies and extended seasonal routes to various destinations in the Atlantic, Pacific and South America regions.

In July, Air Canada began operating to Terminal 3 at Dubai International Airport, marking a significant customer service milestone in its strategic partnership with Emirates. More specifically, Air Canada customers transiting in Dubai between the Americas and the Middle East, Indian subcontinent, Southeast Asia and Africa on Emirates enjoy a seamless and expedited experience with the convenience of remaining in the same terminal.

Cargo

Air Canada Cargo began operating freighter services in 2022 and continued deployments in 2023 to over a dozen destinations, including Toronto, Halifax, St. John's, Miami, Atlanta, Dallas, Quito, Lima, San Juan, Mexico City, Guadalajara, Bogotá, Madrid, Frankfurt, Basel and Liege. Air Canada also enhanced its interline co-operation with Emirates SkyCargo, which allows customers to book interline cargo shipments through the Emirates SkyCargo flights, including between the Americas and Southeast Asia and India, through key European hubs.

At the end of 2023, Air Canada Cargo operated a fleet of seven Boeing 767 freighters compared to three 767 freighters in operation at the end of 2022.

Elevating the Customer

In September, Air Canada was recognized with the 2024 APEX Five Star Global Airline Award. This was the fifth time in six years that Air Canada was awarded an APEX Five Star rating, which is based on customer feedback. Other awards Air Canada received in 2023 for its products and services include:

- Best Airline in Canada from Skytrax World Airline Awards
- Best Airline Staff in Canada from Skytrax World Airline Awards
- Best Low-Cost Airline in Canada (Air Canada Rouge) from Skytrax World Airline Awards
- Favourite Airline in North America from the Trazee Awards (fifth consecutive year)
- Best Airline for Onboard Entertainment from Global Traveler (fifth consecutive year)
- Passenger Choice Award for Best Entertainment in North America from the Airline Passenger Experience Association (APEX)

Aeroplan

Aeroplan rolled out new ways to earn rewards and worked with partners to launch benefits that make it a must-have travel companion for frequent and occasional travellers. The milestones and recognitions included:

- Reaching eight million active members.
- Launching a loyalty partnership with Parkland Corporation.
- Expanding a partnership with Uber Canada, allowing members to also earn points on grocery and retail deliveries with Uber Eats.
- Being recognized with several prestigious Freddie Awards, including Airline Program of the Year, Best Promotion and Best Redemption Ability.
- Earning top honours at Canada's Choice 2023 Travel Loyalty Awards, where Aeroplan was named Top Airline Loyalty Program.

Inclusive Workplace and Impact on Society

Air Canada was named One of Canada's Best Employers for the eighth consecutive year and One of Canada's Best Diversity Employers, both by Forbes. The carrier was also recognized as one of "Montréal's Top Employers" for 2023 in Mediacorp Canada's annual employer survey for the 10th straight year. Air Canada was selected for its employee wellness programs covering both physical and mental health, the philosophy of growing roles and offering diverse opportunities based on various skill sets, along with its internal and external diversity, equity and inclusion initiatives. Air Canada was also recognized as one of Achievers 50 Most Engaged Workplaces for 2023 for the sixth straight year, and received the Outstanding Commitment to Employment Equity Award, the Sector Distinction Award, both under the Employment Equity Achievement Awards, and the 2023 Innovative HR Teams Award by HRD Canada.

Air Canada continued its efforts to enhance its diversity, equity and inclusion practices, including by growing its employee base, providing trainings, fostering partnerships with organizations and participating in local, regional and national activities. These programs and initiatives fall under the DEI holistic framework called CARE, targeting four focus areas: 1) Community outreach; 2) Accountability; 3) Representation; and 4) Engagement and belonging.

Under Air Canada's Accessibility Plan 2023–26 released last June, Air Canada seeks to reduce barriers and make travel simpler, more comfortable and consistently reliable for customers with disabilities. In November 2023, Air Canada announced it was accelerating the Air Canada Accessibility Plan through a series of measures to remove barriers and improve the travel experience for its customers with disabilities. These measures included:

- Investments in new equipment at Canadian airports, such as lifts, to ensure that Air Canada can meet the expectations of its customers.
- Mobility aids will be stored in the aircraft cabin when possible. When mobility aids are stored in the cargo hold, new systems are being put in place to track them in transit, including a process to confirm mobility aids are properly loaded before departure.
- Enhanced training will be supplied to improve all aspects of employee interactions with customers with disabilities, including understanding customer experiences in air travel.
- New senior position of Director, Customer Accessibility who leads a team to manage implementation of the company's accessibility plan as well as provide a resource and common reference point for responsive management of disability issues.

Air Canada also created a Customer Accessibility Advisory Committee consisting initially of four members with disabilities representing four well known Canadian disability organizations. Their role will be to provide guidance and advice on accessibility priorities and initiatives going forward.

The airline continued to promote bilingualism through its strengthened official languages programs, practices and course offerings, all key elements of its Canadian identity and culture.

Regarding annual fundraising events for children and families in need, Air Canada and the Air Canada Foundation reported record outcomes. For instance, in 2023, the Aeroplan points Matching Week raised a record 67 million Aeroplan Points for families needing access to hospital care. It was the most successful points matching campaign in the two-decade history of the initiative The 11th annual Air Canada Foundation Golf Tournament raised a record of nearly $1.3 million in support of charitable organizations that are dedicated to the health and well-being of children and youth across Canada.

Air Canada's Climate Action Plan builds on its existing value streams and activities and is based on four key carbon reduction pillars that are central to the advancement of Air Canada's climate objectives: Fleet and operations; Innovation: SAF and renewable energy; and Carbon reductions and removals. The Plan includes ambitious milestones for Air Canada to achieve its equally ambitious long-term goal of net-zero emissions by 2050. In defining this pathway, 2030 absolute mid-term GHG net reduction targets were set:

- 20% GHG net reductions from air operations by 2030 compared to 2019 baseline.
- 30% GHG net reductions from ground operations by 2030 compared to 2019 baseline.
- $50-million investment for low-carbon technologies to accelerate decarbonization, such as sustainable aviation fuel, and new aircraft technologies.

Additional details on Air Canada's social impact and advancements on its sustainability strategy will be communicated including through Air Canada's upcoming Air Canada Foundation 2023 Impact Report and the 2023 Corporate Sustainability Report.

In pursuit of its *Rise Higher* ambition, in 2024, Air Canada will continue to build upon and leverage its key assets and numerous competitive advantages, including:

- Its talented people and award-winning culture.
- A streamlined, modern, fuel-efficient and versatile fleet with market-leading aircraft configurations.
- A global network, well positioned to meet demand from various customer segments and enhanced by the airline's membership in Star Alliance® and by numerous commercial arrangements.
- A widely recognized and powerful brand.
- A customer experience enhanced by competitive products and services, including the Aeroplan program.
- Air Canada Rouge, a lower-cost leisure carrier, and Air Canada Vacations, a leading Canadian tour operator.
- An expanded cargo offering that leverages network synergies between the passenger and the dedicated freighter fleet.
- New core technologies and other technological improvements.
- A commitment to sustainability.

Fourth Quarter 2023 Financial Summary

The following is an overview of Air Canada's results of operations and financial position for the fourth quarter 2023 compared to the fourth quarter 2022.

- Operating revenues of $5,175 million increased $495 million or 11% on an operated capacity growth of over 9% year over year, close to the guidance provided in Air Canada's news release dated October 30, 2023.
- Operating expenses of $5,096 million increased $388 million or 8%. The increase was due to higher costs in nearly all line items reflecting higher operated capacity and traffic year-over-year, including higher wages, salaries and benefits. The increase was partially offset by lower aircraft fuel expense on a jet fuel price decline.
- Operating income of $79 million, with an operating margin of 1.5%, improved $107 million.
- Adjusted EBITDA of $521 million, with an adjusted EBITDA margin of 10.1%, improved $132 million.
- Net income of $184 million and diluted earnings per share of $0.41 compared to a net income of $168 million and diluted earnings per share of $0.41.
- Adjusted net loss of $44 million and adjusted loss per diluted share of $0.12 compared to an adjusted net loss of $217 million and adjusted loss per diluted share of $0.61.
- Adjusted CASM of 14.25 cents compared to 13.68 cents, an increase of 4.1% driven by higher salaries, wages and benefits expenses, higher maintenance costs and general inflationary pressures on certain line items.
- Net cash flows from operating activities of $985 million increased $338 million.
- Free cash flow of $669 million increased $349 million.

Full Year 2023 Financial Summary

The following is an overview of Air Canada's results of operations and financial position for the full year 2023 compared to the full year 2022.

- Operating revenues of $21,833 million increased $5,277 million or 32% on an approximately 20% growth in operated capacity. The capacity increase was in-line with the guidance provided in Air Canada's news release dated October 30, 2023.
- Operating expenses of $19,554 million increased $2,811 million or 17%. The increase was primarily due to increases in all line items reflecting higher operated capacity and traffic year over year, including, higher salaries, wages and benefits. It also reflected the impact of a favourable maintenance cost adjustment of $159 million that was recorded in the first quarter of 2022.
- Operating income of $2,279 million, with an operating margin of 10.4%, improved $2,466 million.
- Adjusted EBITDA of $3,982 million, with an adjusted EBITDA margin of 18.2%, improved $2,525 million, at the high end of the guidance provided in Air Canada's news release dated October 30, 2023.
- Net income of $2,276 million and diluted earnings per share of $5.96 compared to a net loss of $1,700 million and diluted loss per share of $4.75.

- Adjusted net income of $1,713 million and adjusted earnings per diluted share of $4.56 compared to an adjusted net loss of $988 million and an adjusted loss per diluted share of $2.76.

- Adjusted CASM of 13.49 cents compared to 13.21 cents in 2022, a 2.2% increase driven by higher traffic and selling costs correlated to higher revenues, higher labour costs, a favourable maintenance cost adjustment recorded in 2022, and inflationary pressure on certain line items. This was within the guidance range provided in Air Canada's news release dated October 30, 2023.

- Net cash flows from operating activities of $4,320 million increased $1,952 million.

- Free cash flow of $2,756 million increased $1,960 million.

- Net debt-to-adjusted EBITDA ratio was 1.1 as at December 31, 2023 compared to 5.1 as at December 31, 2022. The improvement was due to the increase in adjusted EBITDA and the $2.9 billion reduction in net debt.

5. RESULTS OF OPERATIONS – 2023 VERSUS 2022

The table and discussion below provide and compare Air Canada's results for the periods indicated.

(Canadian dollars in millions, except where indicated)	Full Year 2023	Full Year 2022	$ Change	% Change
Operating revenues				
Passenger	$ 19,403	$ 14,238	5,165	36
Cargo	924	1,266	(342)	(27)
Other	1,506	1,052	454	43
Total operating revenues	**21,833**	**16,556**	**5,277**	**32**
Operating expenses				
Aircraft fuel	5,318	5,276	42	1
Wages, salaries and benefits	3,955	3,260	695	21
Depreciation, amortization, and impairment	1,703	1,644	59	4
Airport and navigation fees	1,418	1,213	205	17
Sales and distribution costs	1,097	797	300	38
Capacity purchase fees	858	763	95	12
Aircraft maintenance	1,083	706	377	53
Ground package costs	720	474	246	52
Communications and information technology	555	468	87	19
Catering and onboard services	628	425	203	48
Other	2,219	1,717	502	29
Total operating expenses	**19,554**	**16,743**	**2,811**	**17**
Operating income (loss)	**2,279**	**(187)**	**2,466**	
Non-operating income (expense)				
Foreign exchange gain (loss)	389	(732)	1,121	
Interest income	416	168	248	
Interest expense	(944)	(909)	(35)	
Interest capitalized	14	13	1	
Gain on financial instruments recorded at fair value	115	133	(18)	
Loss on debt settlements and modifications	(10)	(14)	4	
Other	(47)	4	(51)	
Total non-operating expense	**(67)**	**(1,337)**	**1,270**	
Income (loss) before income taxes	**2,212**	**(1,524)**	**3,736**	
Income tax recovery (expense)	64	(176)	240	
Net income (loss)	**$ 2,276**	**$ (1,700)**	**$ 3,976**	
Basic earnings (loss) per share	**$ 6.35**	**$ (4.75)**	**$ 11.10**	
Diluted earnings (loss) per share	**$ 5.96**	**$ (4.75)**	**$ 10.71**	
Adjusted EBITDA (1)	**$ 3,982**	**$ 1,457**	**$ 2,525**	
Adjusted pre-tax income (loss) (1)	**$ 1,693**	**$ (952)**	**$ 2,645**	
Adjusted net income (loss) (1)	**$ 1,713**	**$ (988)**	**$ 2,701**	
Adjusted earnings (loss) per share – diluted (1)	**$ 4.56**	**$ (2.76)**	**$ 7.32**	

(1) Adjusted EBITDA, adjusted pre-tax income (loss), adjusted net income (loss), and adjusted earnings (loss) per share are non-GAAP financial measures or non-GAAP financial ratios. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

System Passenger Revenues

In 2023, passenger revenues of $19,403 million increased $5,165 million or over 36% from 2022 with about 14% higher PRASM. These results reflect strong demand for air transportation services in all markets and a better operating environment, in part due to the progressive easing of travel restrictions in Canada in 2022—the last of which were removed in October 2022.

Some of the main drivers for the year-over-year variance included the following:

- Favourable impact of progressive easing of COVID-19-related restrictions in 2022. About 70% of the year-over-year increase in passenger revenues was achieved in the first six months of 2023.
- Strong demand for international travel. Passenger revenues from international markets grew 50% on 26% more capacity—accounting for over 65% of the total year-over-year revenue increase.
- Traffic growth outperformed added capacity resulting in system passenger load factor increasing six percentage points year over year.
- Higher average fares versus 2022. System yields increased 6%.
- Solid demand for premium services. Premium revenues grew more than 37% year over year, representing almost 29% of the total increase in passenger revenues.

The table below provides passenger revenues by geographic region for the periods indicated.

(Canadian dollars in millions)	Full Year			
	2023	2022	$ Change	% Change
Canada	$ 5,106	$ 4,424	$ 682	15.4
U.S. transborder	4,123	3,017	1,106	36.7
Atlantic	6,049	4,381	1,668	38.1
Pacific	2,380	1,118	1,262	112.8
Other	1,745	1,298	447	34.5
System	**$ 19,403**	**$ 14,238**	**$ 5,165**	**36.3**

The table below provides year-over-year percentage changes in passenger revenues and operating statistics for the periods indicated.

	Full Year 2023 versus Full Year 2022					
	Passenger Revenue % Change	Capacity (ASMs) % Change	Traffic (RPMs) % Change	Passenger Load Factor pp Change	Yield % Change	PRASM % Change
Canada	15.4	5.2	11.6	4.9	3.4	9.7
U.S. transborder	36.7	20.0	30.0	6.4	5.2	13.9
Atlantic	38.1	15.6	22.9	5.3	12.3	19.4
Pacific	112.8	81.8	101.8	9.0	5.4	17.0
Other	34.5	16.5	26.4	6.6	6.4	15.5
System	**36.3**	**19.9**	**29.0**	**6.1**	**6.0**	**13.6**

Domestic Passenger Revenues

Domestic passenger revenues increased more than 15% year over year with traffic and capacity increases in almost the entire Domestic network. Yield increased over 3% from 2022 as a result of strong demand in a highly competitive marketplace.

U.S. Transborder Passenger Revenues

U.S. transborder passenger revenues increased about 37% driven by continued strength in U.S. transborder services and in sixth freedom traffic resulting in higher PRASM and yield on a 20% increase in operated capacity. Capacity increased as a result of new, restored and increased U.S. transborder services and improved connection opportunities with Air Canada's international network supporting the sixth freedom traffic strategy.

Atlantic Passenger Revenues

Atlantic passenger revenues increased 38% driven by strong demand for transatlantic travel—to and from Canada as well as sixth freedom traffic—largely driven by a better operating environment and the removal of remaining travel restrictions in Canada in the second half of 2022.

The strong demand, including for premium products, resulted in year-over-year double-digit PRASM and yield gains in nearly all major route groups, with notable strength on routes to continental Europe, despite increased capacity versus 2022.

Pacific Passenger Revenues

Pacific passenger revenues more than doubled year over year as a result of a better operating environment due to the restoration of services to Asia Pacific countries (except for China), especially Japan, following the easing of restrictions in Canada and in these countries. In addition, demand from sixth freedom traffic to the Pacific rebounded compared to 2022 as both our Pacific and transborder networks were restored.

Other Passenger Revenues

Other passenger revenues increased about 35% year over year on strong demand for services to the Caribbean and Central and South America. This largely reflected the favourable impact of the progressive removal of travel restrictions in Canada in 2022.

Cargo Revenues

In 2023, Cargo revenues declined $342 million or 27% from 2022. The decline was due to softness in volume and yield in all markets and to the return of temporarily converted passenger aircraft to passenger operations through the end of the second quarter of 2022. Increased freighter operations to Central and South America and to Europe partially offset the year-over-year decline. At the end of 2023, Air Canada operated seven Boeing 767 freighter aircraft compared to three 767 freighters operated in 2022.

The table below provides cargo revenues by geographic region for the periods indicated.

(Canadian dollars in millions)	Full Year			
	2023	2022	$ Change	% Change
Canada	$ 94	$ 114	$ (20)	(17.7)
U.S. transborder	45	51	(6)	(10.6)
Atlantic	432	556	(124)	(22.2)
Pacific	222	409	(187)	(45.8)
Other	131	136	(5)	(4.0)
System	**$ 924**	**$ 1,266**	**$ (342)**	**(27.0)**

Other Revenues

In 2023, other revenues increased $454 million or 43% from 2022. The increase was largely due to higher ground package revenues at Air Canada Vacations on a combination of higher volume of passengers and higher prices for ground packages. Higher miscellaneous passenger services and onboard purchases on increased traffic and higher non-air revenues related to the Aeroplan program also contributed to the year-over-year growth.

Operating Expenses

In 2023, operating expenses of $19,554 million increased $2,811 million or about 17% from 2022, on about 20% growth in operated capacity. The increase was primarily due to increases in all line items reflecting higher operated capacity and traffic year over year and, to a lesser extent, an unfavourable foreign exchange variance. It also included a $695 million increase in salaries, wages and benefits due to increased headcount and accruals for profit sharing and other wage related items, a favourable maintenance cost adjustment of $159 million that was recorded in the first quarter of 2022 and general inflationary pressures in various line items.

The more notable components of the year-over-year change in operating expenses are described below.

Aircraft Fuel

In 2023, aircraft fuel expense increased 1% from 2022. The increase was driven by 21% more jet fuel litres used on 20% more ASMs. The increase was partially offset by a 14% decline in jet fuel prices—net of an unfavourable foreign exchange variance—and a $51 million net gain from the settlement of jet fuel hedges (in 2022, Air Canada did not have fuel hedging positions in place.) To a lesser extent, the expense related to the Aeroplan carbon offset program for flight rewards also contributed to the increase. This carbon offset program, which was launched in late 2022, compensates the estimated GHG emissions of Aeroplan flight redemptions for itineraries operated by Air Canada, Air Canada Rouge and Air Canada Express.

Wages, Salaries and Benefits

In 2023, wages, salaries and benefits expense increased 21% from 2022. The increase reflects a 17% increase in FTEs required to support planned operations resulting from higher ASMs and accruals for profit sharing and other wage related items. To a lesser extent, higher average salaries contributed to the increase.

Sales and Distribution Costs

In 2023, sales and distribution costs increased 38% from 2022 driven by higher credit card, distribution and commissions, all of which were in line with the 36% growth in passenger revenues.

Capacity Purchase Fees

In 2023, capacity purchase fees increased 12% from 2022 mainly due to higher CPA rates resulting from higher costs incurred by Jazz to operate flights on behalf of Air Canada, including the impact of the new Air Line Pilot Association (ALPA) collective agreement with Jazz (which came into effect on September 1, 2023) increased maintenance costs and an unfavourable foreign exchange variance. This was partially offset by a lower volume of flying year over year as a result of pilot constraints at Jazz. The increase also reflects the agreement with PAL Airlines, which came into effect on July 1, 2023.

Aircraft Maintenance

In 2023, aircraft maintenance expense increased 53% largely due to increased maintenance activities associated with a higher volume of flying year over year and a favourable maintenance cost adjustment of $159 million that was recorded in the first quarter of 2022 as a result of an amended agreement with a third-party maintenance provider. To a lesser extent, an increase in maintenance provisions for leased aircraft that joined the fleet in 2023 contributed to the year-over-year increase.

Ground Package Costs

In 2023, ground package costs increased 52% from 2022 mainly due to higher volume of ground package revenues at Air Canada Vacations. In January 2022, in response to the emergence of the Omicron variant and the associated short-term decline in demand, Air Canada suspended its flights to certain Caribbean destinations from January 24 to April 30, 2022.

Catering and Onboard Services

In 2023, catering and onboard services expenses increased 48% from 2022. The increase was driven by year-over-year growth in traffic, including the impact of changes in traffic mix, and operated capacity. To a lesser extent, general inflationary pressures also contributed to the increase.

Other operating expenses

In 2023, other operating expenses increased 29% driven by a higher volume of flying year over year and, to a lesser extent, inflationary pressures on certain line items.

The following table provides a breakdown of other expenses for the periods indicated.

	Full Year			
(Canadian dollars in millions)	**2023**	**2022**	**$ Change**	**% Change**
Terminal handling	$ 501	$ 367	$ 134	37
Crew cycle	266	207	59	29
Building rent and maintenance	294	229	65	28
Miscellaneous fees and services	218	213	5	2
Remaining other expenses	940	701	239	34
Total other expenses	**$ 2,219**	**$ 1,717**	**$ 502**	**29**

CASM and Adjusted CASM

In 2023, CASM of 19.75 cents declined 2.6% from 2022 driven by the year-over-year ASM increase and was favourably impacted by a 13% decline in jet fuel prices. The unit cost contraction was limited by higher passenger service costs due to higher traffic and higher selling costs correlated to higher revenues, higher salaries, wages and benefits expenses, a favourable maintenance cost adjustment of $159 million recorded in the first quarter of 2022 and general inflationary pressures on certain line items.

Adjusted CASM of 13.49 cents increased 2.2% year over year. The increase was driven by higher passenger service costs due to higher traffic and higher selling costs correlated to higher revenues, higher salaries, wages and benefits expenses, a favourable maintenance cost adjustment of $159 million recorded in the first quarter of 2022 and general inflationary pressures on certain line items.

The following table reconciles CASM to adjusted CASM for the periods indicated.

	Full Year			
(cents per ASM)	**2023**	**2022**	**$ Change**	**% Change**
CASM	**¢ 19.75**	**¢ 20.28**	**¢ (0.53)**	**(2.6)**
Remove:				
Aircraft fuel expense, ground package costs, impairment of assets and freighter costs	(6.26)	(7.07)	0.81	(11.5)
Adjusted CASM	**¢ 13.49**	**¢ 13.21**	**¢ 0.28**	**2.2**

Non-Operating Expense

In 2023, non-operating expenses totalled $67 million, compared to $1,337 million in 2022.

Foreign exchange gains amounted to $389 million compared to losses of $732 million in 2022. The December 31, 2023, closing exchange rate was US$1=1.3243 compared to US$1=$1.3554 at December 31, 2022. With the strengthening of the Canadian dollar, the foreign exchange remeasurement on long-term debt and lease obligations resulted in a gain of $259 million and gains on foreign currency derivatives totalled $139 million in 2023.

Interest expense of $944 million increased $35 million from 2022 driven by the unfavourable impact of higher interest rates year over year on floating-rate debt, and to a lesser extent, an unfavourable foreign exchange variance. The increase was limited as a result of debt repayments made during 2023. For additional information on debt repayments, refer to section 8.2 "Net Debt" of this MD&A.

Interest income of $416 million increased $248 million from 2022 due to higher interest earned on deposits resulting from higher interest rates year over year.

Gain on financial instruments recorded at fair value was $115 million which primarily resulted from fluctuations in the fair value of the embedded derivative on Air Canada's Convertible Notes and of Air Canada's short-term investments portfolio.

Income Tax

In 2023, Air Canada recorded an income tax recovery of $64 million compared to an income tax expense of $176 million in 2022 as shown below. Deferred income tax recovery in the statement of operations partially offset the deferred income tax expense recorded in other comprehensive income related to remeasurements on employee benefit liabilities.

(Canadian dollars in millions)	Full Year	
	2023	2022
Current income tax recovery (expense)	$ 17	$ (47)
Deferred income tax recovery (expense)	47	(129)
Income tax recovery (expense)	**$ 64**	**$ (176)**

6. RESULTS OF OPERATIONS – Q4 2023 VERSUS Q4 2022

The table and discussion below provide and compare Air Canada's results for the periods indicated.

(Canadian dollars in millions, except where indicated)	Fourth Quarter 2023	Fourth Quarter 2022	$ Change	% Change
Operating revenues				
Passenger	$ 4,553	$ 4,062	491	12
Cargo	244	288	(44)	(15)
Other	378	330	48	15
Total operating revenues	**5,175**	**4,680**	**495**	**11**
Operating expenses				
Aircraft fuel	1,391	1,459	(68)	(5)
Wages, salaries and benefits	1,075	892	183	21
Depreciation, amortization, and impairment	442	417	25	6
Airport and navigation fees	350	320	30	9
Sales and distribution costs	253	228	25	11
Capacity purchase fees	223	214	9	4
Aircraft maintenance	311	248	63	25
Ground package costs	177	163	14	9
Communications and information technology	140	127	13	10
Catering and onboard services	161	127	34	27
Other	573	513	60	12
Total operating expenses	**5,096**	**4,708**	**388**	**8**
Operating income (loss)	**79**	**(28)**	**107**	
Non-operating income (expense)				
Foreign exchange gain	72	316	(244)	
Interest income	109	71	38	
Interest expense	(222)	(245)	23	
Interest capitalized	5	5	-	
Gain on financial instruments recorded at fair value	91	44	47	
Loss on debt settlements and modifications	(1)	(31)	30	
Other	(11)	14	(25)	
Total non-operating income	**43**	**174**	**(131)**	
Income before income taxes	**122**	**146**	**(24)**	
Income tax recovery	62	22	40	
Net income	**$ 184**	**$ 168**	**$ 16**	
Basic earnings per share	**$ 0.51**	**$ 0.47**	**$ 0.04**	
Diluted earnings per share	**$ 0.41**	**$ 0.41**	**$ -**	
Adjusted EBITDA (1)	**$ 521**	**$ 389**	**$ 132**	
Adjusted pre-tax (loss) (1)	**$ (47)**	**$ (211)**	**$ 164**	
Adjusted net (loss) (1)	**$ (44)**	**$ (217)**	**$ 173**	
Adjusted loss per share – diluted (1)	**$ (0.12)**	**$ (0.61)**	**$ 0.49**	

(1) Adjusted EBITDA, adjusted pre-tax income (loss), adjusted net income (loss), and adjusted earnings (loss) per share are non-GAAP financial measures or non-GAAP financial ratios. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

System Passenger Revenues

In the fourth quarter of 2023, passenger revenues of $4,553 million increased $491 million or 12% from the fourth quarter of 2022. The increase was driven by higher traffic, operated capacity and yield, most notably in the Pacific, Atlantic and U.S. transborder markets, on strong demand for international air transportation services.

Strong demand for premium products, in all markets, resulted in about 12% higher premium revenues. This increase represented about 28% of the year-over-year growth in passenger revenues.

The table below provides passenger revenues by geographic region for the periods indicated.

(Canadian dollars in millions)	Fourth Quarter			
	2023	2022	$ Change	% Change
Canada	$ 1,245	$ 1,195	$ 50	4.2
U.S. transborder	993	916	77	8.5
Atlantic	1,259	1,096	163	14.8
Pacific	611	412	199	48.1
Other	445	443	2	0.5
System	**$ 4,553**	**$ 4,062**	**$ 491**	**12.1**

The table below provides year-over-year percentage changes in passenger revenues and operating statistics for the periods indicated.

	Fourth Quarter 2023 versus Fourth Quarter 2022					
	Passenger Revenue % Change	Capacity (ASMs) % Change	Traffic (RPMs) % Change	Passenger Load Factor pp Change	Yield % Change	PRASM % Change
Canada	4.2	(2.9)	(0.1)	2.4	4.3	7.3
U.S. transborder	8.5	7.6	7.1	(0.4)	1.3	0.8
Atlantic	14.8	10.6	9.8	(0.6)	4.6	3.8
Pacific	48.1	36.0	41.0	3.1	5.1	8.9
Other	0.5	4.5	2.9	(1.3)	(2.3)	(3.8)
System	**12.1**	**9.3**	**10.1**	**0.7**	**1.8**	**2.6**

Domestic Passenger Revenues

Domestic passenger revenues increased over 4% from the fourth quarter of 2022 driven by higher traffic and capacity in Eastern Canada major route groups. Domestic yield increased more than 4% despite increased competition in the Canadian market. Operated capacity decreased by about 3% mainly due to pilot attrition at our principal regional partner and global supply chain challenges impacting certain aircraft maintenance activities.

U.S. Transborder Passenger Revenues

U.S. transborder passenger revenues increased over 8% from the fourth quarter of 2022 on higher capacity and traffic, notably in the U.S. short- and long-haul markets. Capacity increased as a result of new, restored and increased U.S. transborder services and improved connection opportunities with our international network supporting the sixth freedom traffic strategy.

Atlantic Passenger Revenues

Atlantic passenger revenues increased about 15% from the fourth quarter of 2022 resulting from strong demand for transatlantic services, including for premium products, to and from Canada as well as sixth freedom traffic. This resulted in year-over-year yield and PRASM gains in all major route groups, despite the capacity growth. Capacity increased as a result of new and restored transatlantic routes as well as increased frequencies to certain European destinations, despite the impact of the Tel Aviv route suspension since October 8, 2023.

Pacific Passenger Revenues

Pacific passenger revenues increased about 48% from the fourth quarter of 2022 resulting from a better operating environment and the restoration of services to Asia Pacific countries (except for China), especially Japan, following the easing of restrictions in Canada and in these countries. Demand from sixth freedom traffic to the Pacific rebounded compared to 2022 as both our Pacific and transborder networks were restored.

Other Passenger Revenues

Other passenger revenues increased a half per cent from the fourth quarter of 2022 as the gains from higher traffic and capacity in the Caribbean and Central America were partially offset by lower yields in almost all major route groups.

The table below provides, by market, Air Canada's revenue passenger miles (RPMs) and available seat miles (ASMs) for the periods indicated.

	Fourth Quarter				Full Year			
	2023		2022		2023		2022	
(millions)	**RPMs**	**ASMs**	**RPMs**	**ASMs**	**RPMs**	**ASMs**	**RPMs**	**ASMs**
Canada	4,229	5,034	4,233	5,184	18,224	21,426	16,336	20,373
U.S. transborder	3,744	4,689	3,495	4,356	15,313	18,342	11,781	15,290
Atlantic	6,709	7,989	6,111	7,226	30,823	34,894	25,072	30,188
Pacific	3,333	3,761	2,364	2,765	12,370	13,610	6,128	7,484
Other	2,390	2,966	2,322	2,837	9,072	10,740	7,178	9,223
System	**20,405**	**24,439**	**18,525**	**22,368**	**85,802**	**99,012**	**66,495**	**82,558**

Cargo Revenues

Cargo revenues in the fourth quarter of 2023 declined $44 million or 15% from the fourth quarter of 2022. The decline was primarily due to lower yields in all markets on softness in demand for air cargo services.

The table below provides cargo revenues by geographic region for the periods indicated.

(Canadian dollars in millions)	Fourth Quarter			
	2023	**2022**	**$ Change**	**% Change**
Canada	$ 25	$ 30	$ (5)	(16.0)
U.S. transborder	12	13	(1)	(6.5)
Atlantic	104	145	(41)	(27.4)
Pacific	65	66	(1)	(2.7)
Other	38	34	4	9.9
System	**$ 244**	**$ 288**	**$ (44)**	**(15.2)**

Other Revenues

Other revenues in the fourth quarter of 2023 grew $48 million or 15% from the fourth quarter of 2022. The increase was due to higher ground package revenues at Air Canada Vacations, higher miscellaneous passenger services and onboard purchases on increased traffic and non-air revenues related to the Aeroplan program.

Operating Expenses

In the fourth quarter of 2023, total operating expenses increased 8% from the fourth quarter of 2022, on 9% more capacity, due to increases in nearly all line items reflecting higher operated capacity and traffic year-over-year, including higher wages, salaries and benefits expense. Lower aircraft fuel expense year over year, driven by lower jet fuel prices, partially offset the increase.

The more notable components of the year-over-year change in operating expenses are described below.

<u>Aircraft Fuel</u>

In the fourth quarter of 2023, aircraft fuel expense declined 5% from the fourth quarter of 2022. The decline was driven by a 12% decrease jet fuel prices, despite the impact of a $17 million net hedging loss on jet fuel hedges in the quarter and a $6 million unfavourable foreign exchange variance. The reduction was partially offset by growth in volume of jet fuel litres used on increased flying.

<u>Wages, Salaries and Benefits</u>

In the fourth quarter of 2023, wages, salaries and benefits increased 21% from the fourth quarter of 2022. The increase was due to accruals for profit sharing and other wage related items and a 10% increase in FTEs related to higher flying activity year over year.

<u>Capacity purchase fees</u>

In the fourth quarter of 2023, capacity purchase fees increased 4% from the fourth quarter of 2022 resulting from the agreement with PAL Airlines, which came into effect on July 1, 2023, and higher CPA rates due to higher costs incurred by Jazz to operate flights on behalf of Air Canada, including impact of the new collective agreement between Jazz and ALPA, increased maintenance costs and an unfavourable foreign exchange variance. This was partially offset by lower volume of regional flying as a result of pilot constraints at Jazz.

<u>Aircraft Maintenance</u>

In the fourth quarter of 2023, aircraft maintenance expense increased 25% from the fourth quarter of 2022. This was mainly due to increased maintenance activities, in part associated with a higher volume of flying year over year and to timing of certain maintenance activities. To a lesser extent, inflation-related increases in rates for maintenance activities and an increase in maintenance provisions related to leased aircraft that joined the operating fleet in 2023 also contributed to the increase.

<u>Catering and Onboard Services</u>

In the fourth quarter of 2023, catering and onboard services expenses increased 27% from the fourth quarter of 2022. The increase was driven by year-over-year growth in traffic, including the impact of changes in traffic mix, and operated capacity. To a lesser extent, general inflationary pressures also contributed to the increase.

<u>Other operating expenses</u>

In the fourth quarter of 2023, other operating expenses increased 12% from the same period in 2022 driven by a higher volume of flying, general inflationary pressures on certain line items and an unfavourable foreign exchange variance year over year.

The following table provides a breakdown of other expenses for the periods indicated.

(Canadian dollars in millions)	Fourth Quarter			
	2023	2022	$ Change	% Change
Terminal handling	$ 131	$ 106	$ 25	24
Crew cycle	68	59	9	15
Building rent and maintenance	80	67	13	19
Miscellaneous fees and services	54	67	(13)	(19)
Remaining other expenses	240	214	26	12
Total other expenses	**$ 573**	**$ 513**	**$ 60**	**12**

CASM and Adjusted CASM

In the fourth quarter of 2023, CASM declined 0.9% driven by lower aircraft fuel expenses paired with higher operated capacity year over year. The decline was partially offset by higher salaries, wages and benefits expenses, higher maintenance expenses, higher catering costs as well as general inflationary pressures on various line items.

Adjusted CASM of 14.25 cents increased 4.1% year over year. The increase was driven by higher salaries, wages and benefits expenses, higher maintenance costs and general inflationary pressures on certain line items, including in catering costs.

The following table reconciles CASM to adjusted CASM for the periods indicated.

(cents per ASM)	Fourth Quarter			
	2023	2022	$ Change	% Change
CASM	**¢ 20.85**	**¢ 21.05**	**¢ (0.20)**	**(0.9)**
Remove:				
Aircraft fuel expense, ground package costs, impairment of assets and freighter costs	(6.60)	(7.37)	0.77	(10.4)
Adjusted CASM	**¢ 14.25**	**¢ 13.68**	**¢ 0.57**	**4.1**

Non-Operating Income (Expense)

In the fourth quarter of 2023, total non-operating income amounted to $43 million compared to $174 million in the fourth quarter of 2022.

Foreign exchange gains totalled $72 million compared to gains of $316 million in the fourth quarter of 2022. The December 31, 2023, closing exchange rate was US$1=1.3243 compared to US$1=$1.3577 at September 30, 2023. With the strengthening of the Canadian dollar, the foreign exchange remeasurement on long-term debt and lease obligations resulted in gains of $255 million and were partially offset by losses on foreign currency derivatives of $178 million.

Interest expense of $222 million declined $23 million from the fourth quarter of 2022. The decline was reflected the favourable impact of the debt repayments made in 2023 and was partially offset by higher interest expense on floating-rate debt due to higher interest rates year over year.

7. FLEET

The tables below provide information relating to the aircraft in the operating fleets of Air Canada and Air Canada Rouge as well as the aircraft operated on behalf of Air Canada by regional carriers under the Air Canada Express brand.

Mainline and Air Canada Rouge

The tables below provide information relating to the aircraft in Air Canada's and Air Canada Rouge's operating fleets as at December 31, 2023.

AIR CANADA	At December 31, 2023				
	Number of Operating Aircraft	Total Seats	Average Age	Owned	Leased
Wide-body aircraft					
Boeing 777-300ER	19	418	13.8	11	8
Boeing 777-200LR	6	300	16.4	4	2
Boeing 787-8	8	255	9.6	8	-
Boeing 787-9	30	298	7.0	24	6
Boeing 767-300 freighters	7	-	23.0	5	2
Airbus A330-300	18	295	17.9	8	10
Total wide-body aircraft	88	321	12.8	60	28
Narrow-body aircraft					
Boeing 737 MAX 8	40	169	4.3	31	9
Airbus A321	16	190	20.3	8	8
Airbus A320	19	128	26.8	10	9
Airbus A319	7	125	26.8	7	-
Airbus A220-300	33	137	2.8	33	-
Total narrow-body aircraft	115	153	11.2	89	26
Total Mainline	**203**	**223**	**11.9**	**149**	**54**

AIR CANADA rouge	At December 31, 2023				
	Number of Operating Aircraft	Total Seats	Average Age	Owned	Leased
Narrow-body aircraft					
Airbus A321	17	195	9.1	4	13
Airbus A320	5	168	16.7	-	5
Airbus A319	18	136	25.5	15	3
Total Air Canada Rouge	**40**	**165**	**17.4**	**19**	**21**

Total Mainline & Rouge	**243**	**213**	**12.8**	**168**	**75**

The tables below provide the number of aircraft in Air Canada's operating fleet as at December 31, 2022 and December 31, 2023 as well as Air Canada's planned operating fleet as at the future dates indicated.

AIR CANADA	Actual			Planned			
	Dec. 31, 2022	2023 Fleet Changes	Dec. 31, 2023	2024 Fleet Changes	Dec. 31, 2024	2025 Fleet Changes	Dec. 31, 2025
Wide-body aircraft							
Boeing 777-300ER	18	1	19	-	19	-	19
Boeing 777-200LR	6	-	6	-	6	-	6
Boeing 787-8	8	-	8	-	8	-	8
Boeing 787-9	29	1	30	2	32	-	32
Boeing 787-10	-	-	-	-	-	1	1
Boeing 767-300 freighters	5	2	7	2	9	1	10
Airbus A330-300	16	2	18	1	19	-	19
Total wide-body aircraft	82	6	88	5	93	2	95
Narrow-body aircraft							
Boeing 737 MAX 8	40	-	40	-	40	5	45
Airbus A321XLR	-	-	-	-	-	4	4
Airbus A321	15	1	16	-	16	-	16
Airbus A320	18	1	19	2	21	-	21
Airbus A319	5	2	7	(2)	5	-	5
Airbus A220-300	32	1	33	2	35	7	42
Total narrow-body aircraft	110	5	115	2	117	16	133
Total Mainline	**192**	**11**	**203**	**7**	**210**	**18**	**228**

AIR CANADA rouge	Actual			Planned			
	Dec. 31, 2022	2023 Fleet Changes	Dec. 31, 2023	2024 Fleet Changes	Dec. 31, 2024	2025 Fleet Changes	Dec. 31, 2025
Narrow-body aircraft							
Airbus A321	14	3	17	-	17	-	17
Airbus A320	5	-	5	-	5	-	5
Airbus A319	20	(2)	18	-	18	-	18
Total Air Canada Rouge	**39**	**1**	**40**	**-**	**40**	**-**	**40**

Total Mainline & Rouge	**231**	**12**	**243**	**7**	**250**	**18**	**268**

Air Canada Express

The table below provides the number of aircraft operated on behalf of Air Canada by regional carriers under the Air Canada Express brand, for the dates indicated. The table also provides the planned Air Canada Express fleet as at the future dates indicated.

AIR CANADA EXPRESS	Actual			Planned			
	Dec. 31, 2022	**2023 Fleet Changes**	**Dec. 31, 2023**	**2024 Fleet Changes**	**Dec. 31, 2024**	**2025 Fleet Changes**	**Dec. 31, 2025**
Embraer 175	25	-	25	-	25	-	25
Mitsubishi CRJ-200	15	-	15	(8)	7	-	7
Mitsubishi CRJ-900	35	-	35	-	35	-	35
De Havilland Dash 8-400	39	4	43	-	43	-	43
Total Air Canada Express	**114**	**4**	**118**	**(8)**	**110**	**-**	**110**

8. FINANCIAL AND CAPITAL MANAGEMENT

8.1 LIQUIDITY

Liquidity Risk Management

Air Canada manages its liquidity needs through a variety of strategies, including by seeking to sustain and improve cash from operations and free cash flow, sourcing committed financing for new and existing aircraft, and through other financing activities.

Liquidity needs are primarily related to meeting obligations associated with financial liabilities, capital commitments, ongoing operations, contractual and other obligations, which are further discussed in sections 8.5 "Capital Expenditures and Related Financing Arrangements", 8.6 "Pension Funding Obligations", and 8.7 "Contractual Obligations" of this MD&A. Air Canada monitors and manages liquidity risk by preparing rolling cash flow forecasts for a minimum period of at least twelve months after each reporting period, including under various scenarios and assumptions, monitoring the condition and value of assets available to be used as well as those assets being used as security in financing arrangements, seeking flexibility in financing arrangements, and establishing programs to monitor and maintain compliance with terms of financing agreements.

At December 31, 2023 total liquidity was $10,290 million comprised of cash and cash equivalents, short-term and long-term investments of $9,295 million, and $995 million available under undrawn credit facilities. Cash and cash equivalents include $393 million related to funds held in trust by Air Canada Vacations in accordance with regulatory requirements governing advance sales for tour operators. Over the next 12 months, Air Canada expects to meet its liquidity needs with cash from operations as well as with available cash and cash equivalents, short-term and long-term investments. Liquidity needs, including those related to obligations associated with financial liabilities and capital commitments, may also be supported through new financing arrangements.

8.2 NET DEBT

The table below reflects Air Canada's net debt balances as at December 31, 2023, and as at December 31, 2022.

(Canadian dollars in millions)	December 31, 2023	December 31, 2022	Change
Total long-term debt and lease liabilities	$ 12,996	$ 15,043	$ (2,047)
Current portion of long-term debt and lease liabilities	866	1,263	(397)
Total long-term debt and lease liabilities (including current portion)	**13,862**	**16,306**	**(2,444)**
Less cash, cash equivalents and short and long-term investments	(9,295)	(8,811)	(484)
Net debt (1)	**$ 4,567**	**$ 7,495**	**$ (2,928)**
Adjusted EBITDA (trailing 12 months)	**$ 3,982**	**1,457**	**2,525**
Net debt to adjusted EBITDA ratio (1)	**1.1**	**5.1**	**(4.0)**

(1) Net debt is a capital management measure and a key component of the capital managed by Air Canada and provides management with a measure of its net indebtedness. Net debt to adjusted EBITDA ratio (also referred to as "leverage ratio" in this MD&A) is a non-GAAP financial ratio and is used by Air Canada to measure financial leverage. For additional information on net debt, refer to section 20 "Non-GAAP Financial Measures" of this MD&A.

Net debt to adjusted EBITDA ratio was 1.1 at December 31, 2023, an improvement from the ratio of 5.1 as at December 31, 2022, due to growth in adjusted EBITDA and the reduction in net debt. The decrease in total debt and lease liabilities included $1,276 million of early debt repayments made in 2023—comprised of the $1,112 million from the prepayment of Airbus A220 debt previously used to fund the acquisition of 33 Airbus A220 aircraft and the prepayment of $164 million previously used to fund the acquisition of five Boeing 787-8 aircraft. Greater cash and investments, accumulated through operating cashflows, also contributed to the improvement in net debt.

8.3 WORKING CAPITAL

The table below provides information on Air Canada's working capital balances as at December 31, 2023 and as at December 31, 2022.

(Canadian dollars in millions)	December 31, 2023	December 31, 2022	$ Change
Cash, cash equivalents and short-term investments	$ 8,551	$ 7,988	$ 563
Accounts receivable	1,121	1,037	84
Other current assets	588	640	(52)
Total current assets	**$ 10,260**	**$ 9,665**	**$ 595**
Accounts payable and accrued liabilities	3,328	2,691	637
Advance ticket sales	4,341	4,104	237
Aeroplan and other deferred revenues	1,473	1,295	178
Current portion of long-term debt and lease liabilities	866	1,263	(397)
Total current liabilities	**$ 10,008**	**$ 9,353**	**$ 655**
Net working capital	**$ 252**	**$ 312**	**$ (60)**

Net working capital of $252 million at December 31, 2023 decreased $60 million from December 31, 2022. This was driven by a significant cash outflow due to repayment of long-term debt and lease liabilities and investing activities offset by positive operating cash results.

8.4 CASH FLOW MOVEMENTS

The table below provides the cash flow movements for Air Canada for the periods indicated.

	Fourth Quarter			Full Year		
(Canadian dollars in millions)	2023	2022	$ Change	2023	2022	$ Change
Net cash flows from operating activities	$ 985	$ 647	$ 338	$ 4,320	$ 2,368	$ 1,952
Net cash flows used in financing activities	(332)	(739)	407	(2,368)	(1,612)	(756)
Net cash flows from (used in) investing activities	(289)	137	(426)	(1,827)	(2,498)	671
Effect of exchange rate changes on cash and cash equivalents	(7)	2	(9)	(1)	20	(21)
Increase (decrease) in cash and cash equivalents	**$ 357**	**$ 47**	**$ 310**	**$ 124**	**$ (1,722)**	**$ 1,846**

Net Cash Flows from Operating Activities

Net cash flows from operating activities were better than the 2022 comparative periods driven by better results from operations and strong advance ticket sales.

Net Cash Flows used in Financing Activities

Net cash flows used in financing activities increased $756 million from 2022. The increase was mainly driven by the prepayment of loans which had been used to finance the acquisition of Boeing 787 and Airbus A220 aircraft.

Net Cash Flows from (used in) Investing Activities

Net cash flows used in investing activities decreased by $671 million in 2023 largely due to the net movements between cash and short- and long-term investments. Additions to property, equipment and intangible assets of $1,564 million in 2023, slightly lower than 2022 levels.

Refer to sections 8.2 "Net Debt", and 8.3 "Working Capital" of this MD&A for additional information.

Free Cash Flow

The table below provides the calculation of free cash flow for Air Canada for the periods indicated.

(Canadian dollars in millions)	Fourth Quarter			Full Year		
	2023	2022	$ Change	2023	2022	$ Change
Net cash flows from operating activities	**$ 985**	**$ 647**	**$ 338**	**$ 4,320**	**$ 2,368**	**$ 1,952**
Additions to property, equipment, and intangible assets	(316)	(327)	11	(1,564)	(1,572)	8
Free cash flow (1)	**$ 669**	**$ 320**	**$ 349**	**$ 2,756**	**$ 796**	**$ 1,960**

(1) Free cash flow is a non-GAAP financial measure used by Air Canada as an indicator of the financial strength and performance of its business, indicating how much cash it can generate from operations after capital expenditures. Free cash flow is calculated as net cash flows from operating activities minus additions to property, equipment and intangible assets and net of proceeds from sale and leaseback transactions. Such measure is not a recognized measure for financial statement presentation under GAAP, does not have a standardized meaning, may not be comparable to similar measures presented by other entities and should not be considered a substitute for or superior to GAAP results. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Free cash flow in the fourth quarter and full year 2023 were better than the 2022 comparative periods driven by better net cash flows from operating activities on better operating results and strong advance ticket sales.

8.5 CAPITAL EXPENDITURES AND RELATED FINANCING ARRANGEMENTS

Boeing 787-10 Aircraft

In September 2023, Air Canada announced that it is acquiring 18 Boeing 787-10 aircraft. Deliveries are scheduled to begin in the fourth quarter of 2025 with the last aircraft scheduled for delivery in the first quarter of 2027. The purchase agreement, which includes options for 12 additional Boeing 787-10 aircraft, substitutes for a previously announced agreement to purchase two Boeing 777 freighter aircraft and, as a result, Air Canada will no longer take delivery of the two freighters.

Airbus A321XLR Aircraft

Air Canada is acquiring 30 extra-long range (XLR) versions of the Airbus A321neo aircraft (Airbus A321XLR). Deliveries are scheduled to begin in the third quarter of 2025 with the final aircraft scheduled to arrive in 2029. Of the 30 total aircraft, 15 aircraft will be leased and 15 are being acquired under a purchase agreement with Airbus S.A.S. that includes purchase rights to acquire up to 10 additional aircraft between 2027 and 2031.

Airbus A220-300 Aircraft

Air Canada has an agreement with Airbus Canada for the purchase of Airbus A220-300 aircraft, which provides for:

- Firm orders for 60 Airbus A220-300 aircraft.
- Purchase options for 15 additional Airbus A220-300 aircraft.

Of the above-mentioned 60 firm orders, 33 have been delivered. Deliveries for the 27 remaining firm orders are planned between 2024 and 2027.

Boeing 737 MAX

Air Canada's agreement with Boeing for the purchase of Boeing 737 MAX aircraft provides for firm orders for 40 Boeing 737 MAX 8 aircraft (which have all been delivered) and purchase options for 10 additional Boeing 737 MAX aircraft.

In 2023, Air Canada has entered into lease agreements for five additional Boeing 737 MAX 8 aircraft that are scheduled to enter the operating fleet in 2025.

Boeing 787-9 Aircraft

In 2021, Air Canada exercised options for the purchase of three Boeing 787-9 aircraft. Two 787-9 aircraft were delivered, one in April 2023 and one in January 2024, and the remaining aircraft is scheduled to be delivered in 2024.

Boeing 767 Freighter Aircraft

Air Canada expects to add another three Boeing 767 freighters between 2024 and 2025.

Heart Aerospace ES-30 Electric Aircraft

In 2022, Air Canada finalized a purchase agreement for 30 ES-30 electric-hybrid aircraft under development by Heart Aerospace. Due to the developing design and specifications of the aircraft, the final cost is not yet determinable and is not included in the table below, however the agreement provides for a price cap. The regional aircraft are expected to enter service in 2028.

Capital Commitments

As outlined in the table below, the estimated aggregate cost of all aircraft expected to be delivered and other capital purchase commitments at December 31, 2023 amounted to $12,461 million.

(Canadian dollars in millions)	2024	2025	2026	2027	2028	Thereafter	Total
Committed expenditures	$ 2,000	$ 2,204	$ 4,003	$ 1,397	$ 790	$ 2,067	$ 12,461
Projected planned but uncommitted expenditures	108	332	498	472	505	Not available	Not available
Projected planned but uncommitted capitalized maintenance (1)	517	705	621	455	455	Not available	Not available
Total projected expenditures (2)	**$ 2,625**	**$ 3,241**	**$ 5,122**	**$ 2,324**	**$ 1,750**	**$ Not available**	**Not available**

(1) *Future capitalized maintenance amounts for 2027 and beyond are not yet determinable, however estimates of $455 million have been made for each of 2027 and 2028.*

(2) *U.S. dollar amounts are converted using the December 31, 2023 closing exchange rate of US$1=C$1.3243. The estimated aggregate cost of aircraft is based on delivery prices that include estimated escalation.*

8.6 PENSION FUNDING OBLIGATIONS

Air Canada maintains several defined benefit pension plans, including domestic registered pension plans and supplemental pension plans. Air Canada also sponsors several defined contribution pension plans and pension plans for foreign employees and contributes to some multi-employer pension plans. In addition, Air Canada has plans providing other retirement and post-employment benefits to its employees.

On a preliminary basis, at January 1, 2024, the aggregate solvency surplus in Air Canada's domestic registered pension plans was estimated at $4.3 billion. The final valuations will be completed in the first half of 2024. As permitted by legislation and subject to applicable plan rules, amounts in excess of 105% on a solvency basis can be used to reduce current service contributions under the defined benefit component or to fund the employer contribution to a defined contribution component within the same pension plan.

Total employer defined benefit pension funding contributions (including international and supplemental plans) amounted to $86 million in 2023 and are forecasted to be $101 million in 2024.

Net of the surplus in the defined benefit components which was used to fund the employer contribution to a defined contribution component within the same pension plan, total employer contributions for the defined contribution plans and multi-employer plans amounted to $60 million in 2023 and are forecasted to be $72 million in 2024.

At December 31, 2023, approximately 85% of Air Canada's pension assets in the domestic defined benefit plans were invested in fixed income instruments to mitigate a significant portion of the interest rate (discount rate) risk. Air Canada seeks to maintain a high percentage of long-term fixed income products to hedge pension liabilities.

Pension plan assets

Included in plan assets, for determining the net benefit obligation for accounting purposes, are 17,646,765 (2022 – 17,646,765) shares of Air Canada which were issued to a trust in 2009 in connection with pension funding agreements reached with all of Air Canada's Canadian-based unions. The trust arrangement provides that proceeds of the sale of the trust shares will be retained and applied to reduce future pension solvency deficits, if any should materialize. In addition, for so long as the trust continues to hold at least 2% of Air Canada's issued and outstanding shares, the trustee will have the right to designate one nominee to the Board of Directors of Air Canada (who shall not be a member or officer of any of

Air Canada's Canadian-based unions), subject to completion by Air Canada of its usual governance process for selection and confirmation of director nominees.

With Air Canada's domestic registered plans in a surplus position on a solvency basis, the accounting rules prevent the recognition of the value of the shares held in trust as part of the pension assets. The shares held in trust had a fair value of $330 million at December 31, 2023 (2022 – $342 million), however after giving effect to the asset ceiling, the recognized accounting value of the trust asset is nil.

In November 2021, Air Canada announced that its Canadian unions and the Air Canada Pionairs agreed in principle to permit certain other uses of the proceeds of the shares discussed above. If all conditions are met, shares in the trust will be gradually sold over a period of up to 15 years with the net proceeds from the sales used to make lump sum payments to Canadian pensioners and to fund voluntary separation packages for senior unionized employees and non-executive employees. Pursuant to the agreement in principle, the above-described right to designate one nominee for election to the Board of Directors of Air Canada would continue until the earlier of (i) January 1, 2030, or (ii) the date that Air Canada shares in trust represent 2% or less of Air Canada's issued and outstanding shares. There are several conditions to the completion of the agreement in principle and effecting such sales and payments. These include the conclusion of definitive documentation, and the receipt of all required regulatory and other approvals which remain outstanding. While the satisfaction of the conditions is being pursued, there can be no assurance that these or any other conditions will be satisfied.

8.7 CONTRACTUAL OBLIGATIONS

The table below provides Air Canada's projected contractual obligations as at December 31, 2023, including those relating to interest and principal repayment obligations on Air Canada's long-term debt and lease liabilities and committed capital expenditures.

(Canadian dollars in millions)	2024	2025	2026	2027	2028	Thereafter	Total
Principal							
Long-term debt [(1)]	$ 359	$ 1,092	$ 2,337	$ 1,032	$ 4,222	$ 2,631	$ 11,673
Lease liabilities	507	485	337	279	210	719	2,537
Total principal obligations	**$ 866**	**$ 1,577**	**$ 2,674**	**$ 1,311**	**$ 4,432**	**$ 3,350**	**$ 14,210**
Interest							
Long-term debt	630	604	546	451	323	119	2,673
Lease liabilities	130	102	80	64	50	282	708
Total interest obligations	**$ 760**	**$ 706**	**$ 626**	**$ 515**	**$ 373**	**$ 401**	**$ 3,381**
Total long-term debt and lease liabilities	**$ 1,626**	**$ 2,283**	**$ 3,300**	**$ 1,826**	**$ 4,805**	**$ 3,751**	**$ 17,591**
Committed capital expenditures	**$ 2,000**	**$ 2,204**	**$ 4,003**	**$ 1,397**	**$ 790**	**$ 2,067**	**$ 12,461**
Total contractual obligations [(2)]	**$ 3,626**	**$ 4,487**	**$ 7,303**	**$ 3,223**	**$ 5,595**	**$ 5,818**	**$ 30,052**

(1) Assumes the principal balance of the convertible notes, $363 million (US$274 million), remains unconverted and includes estimated interest payable until maturity in 2025. The full principal balance of $1,273 million for the unsecured credit facility in connection with the Government of Canada financing to support customer refunds is included.

(2) Total contractual obligations exclude commitments for goods and services required in the ordinary course of business. Also excluded are long-term liabilities other than long-term debt and lease liabilities due to reasons of uncertainty of timing of cash flows and items that are non-cash in nature.

8.8 SHARE INFORMATION

The issued and outstanding shares of Air Canada, along with shares potentially issuable, as of the dates indicated below, are as follows:

	December 31, 2023	December 31, 2022
Issued and outstanding shares		
Class A variable voting shares	82,887,375	72,431,001
Class B voting shares	275,581,911	285,931,257
Total issued and outstanding shares	**358,469,286**	**358,362,258**
Class A variable voting and Class B voting shares potentially issuable		
Convertible notes	17,856,599	17,856,599
Stock options	6,642,516	5,304,745
Total shares potentially issuable	**24,499,115**	**23,161,344**
Total outstanding and potentially issuable shares	**382,968,401**	**381,523,602**

Convertible Notes

In June 2020, Air Canada closed US$748 million ($1,011 million) of convertible unsecured notes (Convertible Notes), for net proceeds of $986 million. The Convertible Notes bear interest semi-annually in arrears at a rate of 4.0% per annum and will mature on July 1, 2025, unless earlier repurchased, redeemed or converted. The initial conversion rate of the Convertible Notes is 65.1337 shares per US$1,000 principal amount of Convertible Notes, or an initial conversion price of approximately US$15.35 per share. The Convertible Notes are convertible at the Corporation's election, into cash, or into Class A Variable Voting shares and/or Class B Voting shares of the Corporation, or a combination of cash and shares. The Convertible Notes are convertible prior to the close of business on the business day immediately preceding March 1, 2025 only under the circumstances and subject to satisfaction of the conversion conditions set out in the indenture for the Convertible Notes, and at any time on or after March 1, 2025 until the close of business on the second scheduled trading day immediately preceding July 1, 2025, the maturity date of the Notes, regardless of the foregoing conditions, in each case at the option of the noteholders.

In 2022, Air Canada repurchased and cancelled $635 million (US$473 million) aggregate principal amount of its outstanding Convertible Notes. At December 31, 2023, a total of $363 million (US$274 million) aggregate principal amount of Convertible Notes remains outstanding. At December 31, 2022, the aggregate principal amount of Convertible Notes outstanding was US$274 million.

9. QUARTERLY FINANCIAL DATA

The table below summarizes quarterly financial results for Air Canada for the last eight quarters.

	2022				2023			
(Canadian dollars in millions, except per share figures)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Operating revenues	$ 2,573	$ 3,981	$ 5,322	$ 4,680	$ 4,887	$ 5,427	$ 6,344	$ 5,175
Operating expenses	3,123	4,234	4,678	4,708	4,904	4,625	4,929	5,096
Operating income (loss)	**(550)**	**(253)**	**644**	**(28)**	**(17)**	**802**	**1,415**	**79**
Non-operating income (expense)	**(264)**	**(99)**	**(1,148)**	**174**	**(6)**	**(6)**	**(98)**	**43**
Income (loss) before income taxes	**(814)**	**(352)**	**(504)**	**146**	**(23)**	**796**	**1,317**	**122**
Income tax recovery (expense)	(160)	(34)	(4)	22	27	42	(67)	62
Net income (loss)	**$ (974)**	**$ (386)**	**$ (508)**	**$ 168**	**$ 4**	**$ 838**	**$ 1,250**	**$ 184**
Basic earnings (loss) per share	**$ (2.72)**	**$ (1.08)**	**$ (1.42)**	**$ 0.47**	**$ 0.01**	**$ 2.34**	**$ 3.49**	**$ 0.51**
Diluted earnings (loss) per share	**$ (2.72)**	**$ (1.60)**	**$ (1.42)**	**$ 0.41**	**$ (0.03)**	**$ 2.34**	**$ 3.08**	**$ 0.41**
Adjusted EBITDA (1)	**$ (143)**	**$ 154**	**$ 1,057**	**$ 389**	**$ 411**	**$ 1,220**	**$ 1,830**	**$ 521**
Adjusted pre-tax income (loss) (1)	**$ (740)**	**$ (447)**	**$ 446**	**$ (211)**	**$ (194)**	**$ 656**	**$ 1,278**	**$ (47)**
Adjusted net income (loss) (1)	**$ (747)**	**$ (455)**	**$ 431**	**$ (217)**	**$ (188)**	**$ 664**	**$ 1,281**	**$ (44)**
Adjusted earnings (loss) per share – diluted (1)	**$ (2.09)**	**$ (1.12)**	**$ 1.07**	**$ (0.61)**	**$ (0.53)**	**$ 1.85**	**$ 3.41**	**$ (0.12)**

(1) Adjusted EBITDA, adjusted pre-tax income (loss) and adjusted net income (loss) are non-GAAP financial measures. Adjusted earnings (loss) per share is a non-GAAP financial ratio. For additional information, refer to section 20 "Non-GAAP Financial Measures" of this MD&A.

10. SELECTED ANNUAL INFORMATION

(Canadian dollars in millions, except per share figures)	Full Year 2023	Full Year 2022	Full Year 2021
Operating revenues	$ 21,833	$ 16,556	$ 6,400
Operating expenses	19,554	16,743	9,449
Operating income (loss)	**2,279**	**(187)**	**(3,049)**
Income (loss) before income taxes	2,212	(1,524)	(3,981)
Income tax recovery (expense)	64	(176)	379
Net income (loss)	**$ 2,276**	**$ (1,700)**	**$ (3,602)**
Basic earnings (loss) per share	**$ 6.35**	**$ (4.75)**	**$ (10.25)**
Diluted earnings (loss) per share	**$ 5.96**	**$ (4.75)**	**$ (10.25)**
Adjusted EBITDA (1)	**$ 3,982**	**$ 1,457**	**$ (1,464)**
Adjusted pre-tax income (loss) (1)	**$ 1,693**	**$ (952)**	**$ (3,768)**
Adjusted net income (loss) (1)	**$ 1,713**	**$ (988)**	**$ (3,768)**
Adjusted earnings (loss) per share – diluted (1)	**$ 4.56**	**$ (2.76)**	**$ (10.74)**
Cash, cash equivalents and short-term investments	**$ 8,551**	**$ 7,988**	**$ 8,969**
Total assets	**$ 30,197**	**$ 29,507**	**$ 30,614**
Total long-term liabilities	**$ 19,393**	**$ 21,709**	**$ 23,681**
Total liabilities	**$ 29,401**	**$ 31,062**	**$ 30,605**

(1) Adjusted EBITDA, adjusted pre-tax income (loss) and adjusted net income (loss) are non-GAAP financial measures. Adjusted earnings (loss) per share is a non-GAAP financial ratio. For additional information, refer to section 20 "Non-GAAP Financial Measures" of this MD&A.

11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Gain on Financial Instruments Recorded at Fair Value

The following is a summary of gains (losses) on financial instruments recorded at fair value included in non-operating income (expense) on Air Canada's consolidated statement of operations for the periods indicated.

	Fourth Quarter		Full Year	
(Canadian dollars in millions)	**2023**	**2022**	**2023**	**2022**
Embedded derivative on convertible notes	$ 32	$ 45	64	$ 219
Short-term investments	53	(2)	45	(86)
Other	6	1	6	-
Gain on financial instruments recorded at fair value	**$ 91**	**$ 44**	**115**	**$ 133**

Risk Management

Under its risk management policy, Air Canada manages its market risk through the use of various financial derivative instruments. Air Canada uses these instruments solely for risk management purposes, not for generating trading profit. As such, any change in cash flows associated with derivative instruments is designed to be an economic hedge and offset by changes in cash flows of the relevant risk being hedged.

The fair values of derivative instruments represent the amount of the consideration that could be exchanged in an arm's length transaction between willing parties who are under no compulsion to act. The fair value of these derivatives is determined using prices in active markets, where available. When no such market is available, valuation techniques such as discounted cash flow analysis are applied. The valuation technique incorporates all factors that would be considered in setting a price, including Air Canada's own credit risk as well as the credit risk of the counterparty.

Fuel Price Risk Management

Fuel price risk is the risk that future cash flows will fluctuate because of changes in jet fuel prices. To manage its exposure to jet fuel prices and to help mitigate volatility in operating cash flows, the Corporation can elect to enter into derivative contracts with financial intermediaries. The Corporation may use derivative contracts based on jet fuel, heating oil and crude-oil based contracts. The Corporation's policy permits hedging of up to 75% of the projected jet fuel purchases for the current calendar year, 50% of the projected jet fuel purchases for the next calendar year, and 25% of projected jet fuel purchases for any calendar year thereafter. These are maximum (but not mandated) limits. There is no minimum monthly hedging requirement. There are regular reviews to adjust the strategy in light of market conditions.

During 2023, the Corporation purchased jet fuel call options covering a portion of fuel exposure in the second half of 2023. The cash premium related to these contracts was $44 million. Premium costs and any hedging gains and losses are reclassified from other comprehensive income to Aircraft fuel expense on settlement of the derivatives. Fuel derivative contracts cash settled with a fair value of $95 million in favour of the Corporation, with a net hedging gain of $51 million recorded in Aircraft fuel expense. No hedge ineffectiveness was recorded. There were no outstanding fuel derivatives as at December 31, 2023 and there was no fuel hedging activity during 2022.

Foreign Exchange Risk

Air Canada's financial results are reported in Canadian dollars, while a large portion of its expenses, debt obligations and capital commitments are in foreign currencies, primarily in U.S. dollars. Foreign exchange risk is the risk that fluctuations in foreign exchange rates may have on operating results and cash flows. Air Canada's risk management objective is to reduce cash flow risk related to foreign denominated cash flows.

Air Canada generates certain sales in U.S. dollars and in other foreign currencies which are converted to U.S. dollars under Air Canada's risk management program. In 2023, these net operating cash inflows totalled approximately US$4.2 billion and U.S. denominated operating costs amounted to approximately US$7.8 billion. Non-operating cash outflows in U.S. dollars, primarily related to interest payments on U.S. dollar denominated debt and net financing outflows, amounted to approximately US$2.2 billion. In 2023, this resulted in a U.S. dollar net cash flow exposure of approximately US$5.8 billion.

Air Canada has a target coverage of 60% on a rolling 18-month basis to manage the net U.S. dollar cash flow exposure described above utilizing the following risk management strategies:

- Holding U.S. dollar cash reserves as an economic hedge against changes in the value of the U.S. dollar. U.S. dollar cash, short and long-term investment balances as at December 31, 2023 amounted to $1,123 million (US$845 million)—$693 million (US$511 million) as at December 31, 2022. A portion of the cash and investment reserves are an economic hedge against long-term U.S. dollar debt while the remainder of the cash is operational cash and investment reserves which are applied against the rolling 18-month net U.S. dollar cash flow exposure. In 2023, a loss of $18 million (gain of $72 million in 2022) was recorded in Foreign exchange gain (loss) reflecting the change in Canadian equivalent market value of the U.S. dollar cash, short and long-term investment balances held.

- Locking in the foreign exchange rate through the use of a variety of foreign exchange derivatives which have maturity dates corresponding to the forecasted dates of U.S. dollar net outflows.

The level of foreign exchange derivatives entered into and their related maturity dates are dependent upon a number of factors, which include the amount of foreign revenue conversion available, U.S. dollar net cash outflows, as well as the amount attributed to aircraft and debt payments. Based on the notional amount of currency derivatives outstanding at December 31, 2023, as further described below, approximately 63% of net U.S. cash outflows are hedged for 2024 and 39% for 2025, resulting in derivative coverage of 56% over the next 18 months, as of December 31, 2023. Operational U.S. dollar cash and investment reserves combined with derivative coverage results in 60% coverage over the next 18 months as of December 31, 2023.

As at December 31, 2023, Air Canada had outstanding foreign currency options and swap agreements, settling in 2024 and 2025, to purchase at maturity $5,982 million (US$4,542 million) of U.S. dollars at a weighted average rate of $1.3089 per US$1.00 (2022 – $5,798 million (US$4,310 million) with settlements in 2023 and 2024 at a weighted average rate of $1.2986 per $1.00 U.S. dollar). Air Canada also has protection in place to sell a portion of its excess Euros, Sterling, YEN, and AUD (EUR €276 million, GBP £166 million, JPY ¥14,797 million, and AUD $124 million) which settle in 2024 and 2025 at weighted average rates of €1.1292, £1.2790, ¥0.0075, and AUD $0.6920 per $1.00 U.S. dollar, respectively (as at December 31, 2022 – EUR €198 million, GBP £244 million, JPY ¥17,405 million, CNH ¥355 million and AUD $126 million with settlement in 2023 and 2024 at weighted average rates of €1.0828, £1.2467, ¥0.0082, ¥0.1419, and AUD $0.7072 respectively per $1.00 U.S. dollar).

The hedging structures put in place have various option pricing features, such as knock-out terms and profit cap limitations, and based on the assumed volatility used in the fair value calculation, the net fair value of these foreign currency contracts as at December 31, 2023 was $165 million in favour of the counterparties (2022 – $140 million in favour of the counterparties). These derivative instruments have not been designated as hedges for accounting purposes and are recorded at fair value. During 2023, a gain of $139 million was recorded in Foreign exchange gain (loss) related to these derivatives (2022 – $174 million gain). In 2023, foreign exchange derivative contracts cash settled with a net fair value of $163 million in favour of Air Canada (2022 – $46 million in favour of the Corporation).

Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Air Canada enters into both fixed and floating rate debt and also leases certain assets where the rental amount fluctuates based on changes in short term interest rates. Air Canada manages interest rate risk on a portfolio basis and seeks financing terms in individual arrangements that are most advantageous taking into account all relevant factors, including credit margin, term and basis. The risk management objective is to minimize the potential for changes in interest rates to cause adverse changes in cash flows to Air Canada. The cash and short-term investment portfolio which earns a floating rate of return is an economic hedge for a portion of the floating rate debt.

The ratio of fixed to floating rate obligations outstanding is designed to maintain flexibility in the Corporation's capital structure and is based upon a long-term objective of 60% fixed and 40% floating but allows flexibility to adjust to prevailing market conditions. The ratio at December 31, 2023 was 75% fixed and 25% floating (71% and 29%, respectively as at December 31, 2022).

12. ACCOUNTING POLICIES

Information on Air Canada's accounting policies is provided in Note 2 of Air Canada's audited consolidated financial statements and notes for 2023, including future changes in accounting policies for amendments to standards not yet effective.

Amendments to IAS 1, Presentation of Financial Statements – Disclosure of Accounting Policies

In February 2021, the IASB issued amendments to IAS 1 that require entities to disclose material accounting policy information instead of significant accounting policies. The amendments are effective for annual periods beginning on or after January 1, 2023. The Corporation adopted this amendment effective the 2023 annual period with no substantial impact on the disclosure of its accounting policies.

IAS 12 Income Taxes

In May 2023, the IASB issued an amendment to IAS 12. The amendment addresses accounting for the global minimum tax as outlined in the two-pillar plan for international tax reform developed by the Organisation for Economic Co-operation and Development. The objective of the tax reform is to ensure that large multinational enterprises are subject to a minimum income tax rate of 15% in each jurisdiction they operate. The amendment to IAS 12 includes temporary mandatory relief from recognizing and disclosing deferred taxes related to the implementation of Pillar Two global minimum tax rules. As of December 31, 2023, the Pillar Two legislation has not yet been enacted or substantively enacted in any of the jurisdictions where the Corporation has a constituent entity for the purposes of Pillar Two. As such, the Corporation has yet to apply the temporary exemption. The Corporation will disclose known or reasonably estimable information related to the Corporation's exposure to Pillar Two income taxes when it is enacted or substantively enacted in a jurisdiction where the Corporation has a constituent entity and will disclose separately current tax related to Pillar Two income taxes when it is in effect.

13. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Critical accounting estimates are those estimates of management that are most important to the portrayal of Air Canada's financial condition and results of operations. They require management's most difficult, subjective or complex judgments, often because of the need to make estimates and judgments about the effect of matters that are inherently uncertain. Actual results could differ materially from those estimates and judgments.

Significant estimates and judgments made in the preparation of Air Canada's consolidated financial statements include, but are not limited to, the following areas.

Impairment Considerations on Long-lived Assets

When required, an impairment test is performed by comparing the carrying amount of the asset or cash-generating unit to their recoverable amount, which is calculated as the higher of an asset's or cash-generating unit's fair value less costs to dispose and its value in use. Fair value less costs to dispose may be calculated based upon a discounted cash flow analysis, which requires management to make a number of significant market participant assumptions including assumptions relating to cash flow projections, discount rates and future growth rates.

Aeroplan Loyalty Program

Loyalty program accounting requires management to make several estimates including the ETV of Aeroplan Points issued and the breakage on Aeroplan Points. The ETV of Aeroplan Points issued is determined based on the value a passenger receives by redeeming Points for a ticket rather than paying cash. This ETV is estimated with reference to historical Aeroplan redemptions as compared to equivalent ticket purchases after considering similar fare conditions, advance booking periods and other relevant factors including the selling price of Points to third parties. ETV estimates and assumptions are considered for updates at least annually. A change in the ETV rate is accounted for prospectively.

Breakage represents the estimated Points that are not expected to be redeemed. Breakage is estimated by management based on the terms and conditions of membership and historical accumulation and redemption patterns, as adjusted for changes to any terms and conditions or other circumstances that may affect future redemptions. Management uses statistical and simulation models to estimate breakage. A change in assumptions as to the number of Points expected to be redeemed could have a significant impact on revenue in the year in which the change occurs. Given the unique impact of the COVID-19 pandemic had on travel demand and consumer spending patterns, and considering the launch of the new Aeroplan program in 2020 and the special benefits and accommodations for Aeroplan Members in response to the COVID-19 pandemic, the breakage estimate is unchanged in 2023 and is based on a qualitative update of the prior assessment. In addition, the estimate is based on management's long-term expectations of breakage over the life of the program.

As at December 31, 2023, the Aeroplan points deferred revenue balance was $3,562 million. For illustrative purposes, a hypothetical 1% change in the number of outstanding points estimated to be redeemed would result in an approximate impact of $36 million on revenue with a corresponding adjustment to Aeroplan deferred revenue.

Breakage

Breakage estimates and resulting amount of breakage revenues recorded are estimated based on historical breakage patterns and are subject to measurement uncertainty. Estimates of breakage may vary in future periods. These estimates have been impacted by the COVID-19 pandemic including: (i) flight cancellations, (ii) the conversion of certain tickets into non-expiring travel vouchers for flights that were cancelled with travel dates after February 1, 2020 and purchased before April 13, 2021, and (iii) changes in ticket usage and exchange patterns.

Depreciation and Amortization Period for Long-lived Assets

The Corporation makes estimates about the expected useful lives of long-lived assets and the expected residual value of the assets based on the estimated current and future fair values of the assets, the Corporation's fleet plans and the cash flows they generate. Changes to these estimates, which can be significant, could be caused by a variety of factors, including changes to maintenance programs, changes in jet fuel prices and other operating costs, changes in utilization of the aircraft, and changing market prices for new and used aircraft of the same or similar types. Estimates and assumptions are evaluated at least annually. Generally, these adjustments are accounted for on a prospective basis, through depreciation and amortization expense. For the purposes of sensitivity analysis on these estimates, a 50% reduction to residual values on aircraft with remaining useful lives greater than five years results in an increase of $14 million to annual depreciation expense. For aircraft with shorter remaining useful lives, the residual values are not expected to change significantly.

Maintenance Provisions

The recording of maintenance provisions related to return conditions on aircraft leases requires management to make estimates of the future costs associated with the maintenance events required under the lease return condition and estimates of the expected future maintenance condition of the aircraft at the time of lease expiry. These estimates take into account current costs of these maintenance events, estimates of inflation surrounding these costs as well as assumptions surrounding utilization of the related aircraft. Any difference in the actual maintenance cost incurred at the end of the lease and the amount of the provision is recorded in Aircraft maintenance expense in the period. The effect of any changes in estimates, including changes in discount rates, inflation assumptions, cost estimates or lease expiries, is recognized as an adjustment to the right-of-use asset.

Income Taxes

Since 2020, the net deferred income tax assets related to unused tax losses and other deductible temporary differences have not been recognized. As a result of the COVID-19 pandemic, there was considerable negative evidence relating to losses that were incurred at that time and assumptions as to the timing of reversal of temporary differences include expectations about the future results of operations and future cash flows. Management continues to assess the available positive and negative evidence to estimate whether sufficient future taxable income will be generated to permit use of the existing deferred tax assets. Deferred tax assets have only been recognized to the extent of taxable temporary differences expected to reverse and generate taxable income against which the deferred tax assets can be utilized. The future income tax deductions underlying the unrecognized deferred income tax assets remain available for use in the future to reduce taxable income.

Employee Future Benefits

The cost and related liabilities of the Corporation's pension, other post-retirement and post-employment benefit programs are determined using actuarial valuations. The actuarial valuations involve assumptions and estimates including discount rates and mortality assumptions. Also, due to the long-term nature of these programs, such estimates are subject to significant uncertainty.

Assumptions

Management is required to make estimates about actuarial and financial assumptions to determine the cost and related liabilities of Air Canada's employee future benefits.

Discount Rate

The discount rate used to determine the pension obligation was determined by reference to market interest rates on corporate bonds rated "AA" or better with cash flows that approximate the timing and amount of expected benefit payments.

Future Increases in Compensation

Estimates surrounding assumptions of future increases in compensation are based upon the current compensation policies, Air Canada's long-range plans, labour and employment agreements and economic forecasts.

Mortality Assumptions

Mortality tables and improvement scales issued by the Canadian Institute of Actuaries (revised in 2014) were taken into account in selecting management's best estimate mortality assumption used to calculate the accrued benefit obligation as at December 31, 2023 and 2022.

The weighted average assumptions used to determine the Corporation's accrued benefit obligations and cost are as follows:

	Pension Benefits		Other Employee Future Benefits	
	2023	2022	2023	2022
Discount rate used to determine:				
Net interest on the net defined benefit obligation for the year ended December 31	5.28%	3.20%	5.28%	3.20%
Service cost for the year ended December 31	5.28%	3.37%	5.28%	3.37%
Accrued benefit obligation as at December 31	4.64%	5.28%	4.64%	5.28%
Rate of future increases in compensation used to determine:				
Accrued benefit cost and service cost for the year ended December 31	2.75%	2.50%	Not applicable	Not applicable
Accrued benefit obligation as at December 31	2.75%	2.75%	Not applicable	Not applicable

Sensitivity Analysis

Sensitivity analysis is based on changing one assumption while holding all other assumptions constant. In practice, this may be unlikely to occur, and changes in some of the assumptions may be correlated. When calculating the sensitivity of the defined benefit obligation to variations in significant actuarial assumptions, the same method (present value of the defined benefit obligation calculated with the projected unit credit method at the end of the reporting period) has been applied as for calculating the liability recognized in the consolidated statement of financial position.

Sensitivity analysis on 2023 pension expense, net interest relating to pension benefit liabilities and pension obligation, based on different actuarial assumptions with respect to discount rate is set out below. The effects on each pension plan of a change in an assumption are weighted proportionately to the total plan obligation to determine the total impact for each assumption presented.

	0.25 Percentage Point	
(Canadian dollars in millions)	**Decrease**	**Increase**
Discount rate on obligation assumption		
Pension expense	$ 12	$ (11)
Net interest relating to pension benefit liabilities	(1)	-
Total	**$ 11**	**$ (11)**
Increase (decrease) in pension obligation	**$ 591**	**$ (573)**

The increase (decrease) in the pension obligation for a 0.25-percentage-point change in the discount rate relates to the gross amount of the pension liabilities and is before the impact of any change in plan assets. As at December 31, 2023, approximately 85% of Air Canada's pension assets were invested in fixed income instruments to mitigate a significant portion of the interest rate (discount rate) risk.

An increase of one year in life expectancy would increase the pension benefit obligation by $431 million.

Assumed health care cost trend rates impact the amounts reported for the health care plans. A 4.50% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2023 and thereafter (2022 – 4.75% and decrease gradually to 4.5% by 2023). A one-percentage-point increase in assumed health care trend rates would have increased the total of current service and interest costs by $5 million and the obligation by $62 million. A one-percentage-point decrease in assumed health care trend rates would have decreased the total of current service and interest costs by $4 million and the obligation by $64 million.

A 0.25-percentage-point decrease in discount rate for other employee future benefits would have increased the total of current and interest costs by less than $1 million and the obligation by $36 million. A 0.25-percentage-point increase in discount rate would have decreased the total of current and interest costs by less than $1 million and the obligation by $34 million.

14. OFF-BALANCE SHEET ARRANGEMENTS

Guarantees

Air Canada participates in fuel facility arrangements operated through nine Fuel Facility Corporations, and three aircraft de-icing service facilities, along with other airlines that contract for fuel and de-icing services at various major airports in Canada. These entities operate on a cost recovery basis. The aggregate debt of these entities that has not been consolidated by the Corporation under IFRS 10 Consolidated Financial Statements is approximately $1,215 million as at December 31, 2023 (December 31, 2022 – $1,181 million), which is Air Canada's maximum exposure to loss before taking into consideration the value of the assets that secure the obligations and any cost sharing that would occur among the other contracting airlines. Air Canada views this loss potential as remote. Each contracting airline participating in these entities shares pro rata, based on system usage, in the guarantee of this debt. The maturities of these debt arrangements vary but generally extend beyond five years.

Indemnification Agreements

In the ordinary course of Air Canada's business, Air Canada enters into a variety of agreements, such as real estate leases or operating agreements, aircraft financing or leasing agreements, technical service agreements, and director/officer contracts, and other commercial agreements, some of which may provide for indemnifications to counterparties that may require Air Canada to pay for costs and/or losses incurred by such counterparties. Air Canada cannot reasonably estimate the potential amount, if any, it could be required to pay under such indemnifications. Such amount would also depend on the outcome of future events and conditions, which cannot be predicted. While certain agreements specify a maximum potential exposure, certain others do not specify a maximum amount or a limited period. Historically, Air Canada has not made any significant payments under these indemnifications.

Air Canada expects that it would be covered by insurance for most extra-contractual liabilities and certain contractual indemnities.

15. RELATED PARTY TRANSACTIONS

At December 31, 2023, Air Canada had no transactions with related parties as defined in the CPA Handbook, except those pertaining to transactions with key management personnel in the ordinary course of their employment or directorship agreements.

16. SENSITIVITY OF RESULTS

Air Canada's financial results are subject to many different internal and external factors which can have a significant impact on operating results. The following table describes, on an indicative basis, the financial impact that changes in fuel prices and the value of the Canadian dollar would generally have had on Air Canada's past operating results. An equivalent but opposite movement of the sensitivity factor in the table below would have generally resulted in a similar but opposite impact. These guidelines were derived from 2023 levels of activity and are based on management estimates. The impacts are not additive, do not reflect the interdependent relationship of the elements and may not be indicative of future trends or results which may vary significantly due to a wide range of factors many of which are beyond the control of Air Canada.

Key Variable	2024 Measure	Sensitivity Factor	Favourable/ (Unfavourable) Estimated Operating Income Impact/Pre-tax Income (Canadian dollars in millions)	
Fuel				
Fuel – Jet fuel price (US$/barrel) (1)	$129.0	US$1/barrel increase	$	(45)
Fuel – Jet fuel price (C$/litre) (1)	$1.13	1% increase	$	(58)
Currency Exchange				
C$ to US$	US$1=C$1.33	1 cent appreciation (i.e. from $1.34 to $1.33 per US$)		
		Operating income (2)	$	36
		Net interest expense		5
		Revaluation of long-term debt and lease liabilities, U.S. dollar cash, cash equivalents and short-term investments, and other long-term monetary items, net		78
		Remeasurement of outstanding currency derivatives		(45)
		Pre-tax income impact	**$**	**74**

(1) Excludes the impact of carrier surcharges and fuel hedging (if any).
(2) The operating income impact of currency exchange movements is before the impact of hedging activities, such as through the use of foreign currency derivatives and holding U.S. dollar cash reserves. The gains and losses related to these hedging activities are recorded in non-operating income (expense) on Air Canada's consolidated statement of operations.

17. ENTERPRISE RISK MANAGEMENT AND GOVERNANCE

Overview

The management of opportunities and risks is an integral part of Air Canada's business processes. Strategic decisions are made by the executive team with consideration of risk implications to the business and its stakeholders. Risks which may be material to Air Canada are identified and monitored on an on-going basis through Air Canada's Enterprise Risk Management (ERM) program which provides insight on a regular basis to the Board of Directors through the Board's Audit, Finance and Risk Committee.

Board Oversight

Risk management is an integral part of Air Canada's corporate governance. The Board of Directors has established board committees (Audit, Finance and Risk Committee; Safety, Health, Environment and Security Committee; Governance and Nominating Committee; and Human Resources, Compensation and Pension Committee) to assist in the oversight responsibilities.

Risk information is reviewed by the Board or the relevant Board committee on a quarterly basis. In addition, Board committees review and discuss with management, on a regular basis, all key enterprise risk exposures based on their respective terms of reference set out in committee charters and the steps taken that seek to monitor/control and mitigate those exposures to satisfy themselves as to the effective risk management of the individual risks. These processes seek to appropriately mitigate rather than eliminate risk.

The Audit, Finance and Risk Committee is responsible for the oversight of the ERM program and the work carried out by the Corporate Audit and Advisory department, as stated in its committee charter.

ERM risk reporting is maintained by the Corporate Audit and Advisory department, which provides an independent update as to the state of each enterprise risk on a quarterly basis.

Risk Management Framework and Structure

Air Canada's enterprise risk management framework has been developed to support governance and oversight over Air Canada's most important strategic risks and is aligned to the ISO 31000 standard and COSO ERM 2017 framework.

Policies and processes are in place to manage specific risks such as safety, security, fraud, cybersecurity, privacy, environment and fuel price.

Sound business practices and ethical behaviour are also fundamental to Air Canada's risk governance culture. Air Canada has in place (and updates, as required) a Corporate Policy and Guidelines on Business Conduct (Code of Conduct), which sets out guiding principles and ethical standards that apply to all Air Canada's corporate activities. A confidential, anonymous reporting process and ethics committee are also in place to oversee adherence to the Code of Conduct.

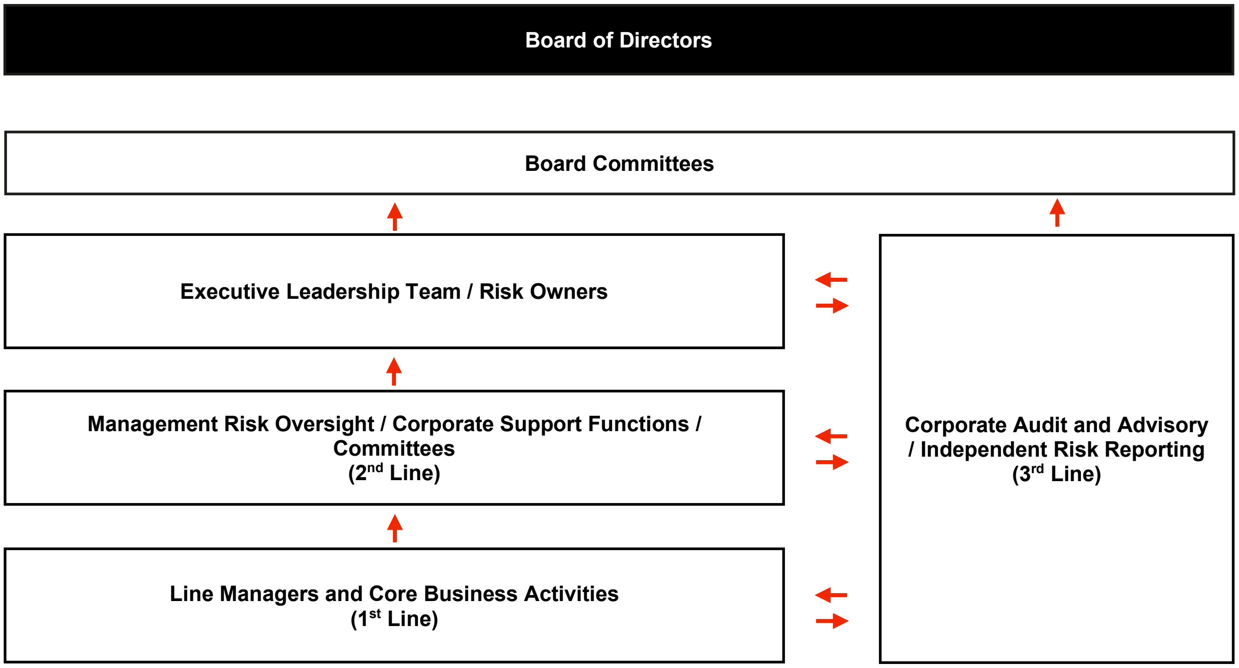
Air Canada's risk management structure is aligned with the "Three Lines Model" approach to risk management:

1st line - Business functions are expected to integrate risk management when performing their day-to-day core commercial and operational activities.

2nd line - Support functions establish policies, provide guidance and expertise, and risk oversight (e.g. Safety, Security, Legal and Compliance, Finance/Treasury/Tax, Sourcing and Procurement, Government Affairs, People, Environment, IT Operations and Cybersecurity).

3rd line - Corporate Audit and Advisory department provides an independent and objective perspective on Air Canada's governance, risk management practices and controls.

Air Canada's ERM and governance structure is as follows:



Although the risk management framework described in this section is aligned with industry best practices, there can be no assurance that it will be sufficient to prevent the occurrence of events that could have a material adverse effect on our financial position, financial performance, cash flows, business or reputation.

18. RISK FACTORS

The risks described below should be read carefully when evaluating Air Canada's business and the forward-looking statements contained in this report and other statements Air Canada may make from time to time. Any of these risks, individually or in combination, could materially and adversely affect Air Canada's business, results from operations, financial condition as well as the outcome of matters as to which forward-looking statements are made. Should a risk materialize, circumstances at the time may also cause that risk to have a different impact than that which might otherwise have been expected. These risks may not be the only ones faced by Air Canada. Other risks of which Air Canada is not aware or which Air Canada deems not to be material may surface and have a material and adverse impact on Air Canada, its business, results from operations, financial condition and the outcome of matters as to which forward-looking statements are made.

Economic and geopolitical conditions – Changes in economic and geopolitical conditions could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada's results from operations are sensitive to and may be significantly impacted by economic and geopolitical conditions, which may also impact overall demand for air transportation or to or from certain destinations, the ability to operate to destinations or the viability or routes, operating costs and revenues, fuel cost and availability, foreign exchange costs, tax costs and the costs and availability of capital and supplies. Any prolonged or significant impact arising from economic and geopolitical conditions, including in relation to conflicts involving Israel and Hamas, or Russia and Ukraine, or other geopolitical conflicts, and civil unrest, as well as related responses of various governments and authorities (or lack thereof), infectious diseases, weakness of the Canadian, U.S. or world economies, inflation, changes to political, economic, fiscal or trade relationships within or between jurisdictions where Air Canada operates flights or does business, or threatened or actual conflicts or outbreaks of hostilities in or adjacent to regions Air Canada serves or over which it operates flights or does business could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Operating results – Air Canada may sustain significant losses and not be able to successfully achieve and/or sustain positive net profitability or realize the objectives of any or all its initiatives.

A variety of factors, including economic conditions and other factors described in this MD&A, may result in Air Canada incurring significant losses. The airline industry has historically been characterized by low profit margins and high fixed costs, and the costs of operating a flight do not vary significantly with the number of passengers carried. Therefore, a change in the number of passengers, fare pricing, margins or traffic mix, or increased costs, could have a significant impact on Air Canada's operating and financial results. Due to the competitive nature of the airline industry and customer sensitivity to travel costs, Air Canada may not be able to pass on cost increases to its customers. Despite a focus on improving resiliency to downturns in its business as well as ongoing and planned strategic and business initiatives, Air Canada may not be able to successfully achieve and/or sustain positive net profitability or realize all of its objectives, including those that seek to increase revenues, decrease costs, improve margins, profitably deploy additional capacity, generate sufficient returns on its capital expenditures or offset or mitigate risks facing Air Canada, including those described in this MD&A.

Fares and market demand – Fluctuations in fares and demand for air travel could materially adversely impact Air Canada, its business, results from operations and financial condition.

Air Canada fares and passenger demand, like those of other airlines, have fluctuated significantly in the past and may fluctuate significantly in the future, Air Canada cannot predict with certainty market conditions and the fares that Air Canada may be able to charge. Customer expectations and perception can change rapidly due to many factors, and the demand for lower fares or alternative modes of transportation may impact revenues. Travel, especially leisure travel, is a discretionary consumer expense. Demand for business and premium travel is also impacted by a variety of factors such as economic and geopolitical conditions. Many factors such as depressed economic conditions, geopolitical instability, infectious diseases, and concerns about the environmental impacts of air travel and tendencies toward less environmentally impactful travel, could each have the effect of reducing demand for air travel and fares and could materially adversely impact Air Canada, its business, results from operations and financial condition.

Competition – Air Canada operates in a highly competitive environment and faces increasing competition in Canada, North America and internationally.

Air Canada operates within a highly competitive industry and continuously encounters substantial price competition. Carriers, including low-cost, ultra-low-cost, domestic, U.S. and foreign carriers, have entered, announced their intention to enter or continue to enter or expand into markets Air Canada operates in or plans to operate in, including domestic, U.S. transborder, international and leisure-oriented markets, as well as cargo transportation markets.

Carriers against which Air Canada competes, including U.S. and Canadian carriers, may undergo (and some have undergone) substantial reorganizations (including by way of merger with or acquisition by another carrier or entity), creating greater access to capital, reduced levels of indebtedness, lower operating costs and other competitive advantages. Consolidation within the airline industry and carriers increasingly entering into integrated commercial cooperation arrangements (including with multi-modal operators) may also strengthen the ability of carriers to compete.

The prevalence of internet travel websites and other travel product distribution channels has also resulted in a substantial increase in new routings and discounted and promotional fares initiated by Air Canada's competitors. Competitors also continue to pursue commissions and incentive actions and, in many cases, increase these payments. Air Canada's ability to reduce its fares in order to effectively compete is dependent on its ability to achieve acceptable operating margins and may be limited by applicable laws or government policies to encourage competition.

Increased competition, from existing or new competitors, including competitors entering into new or expanded joint ventures and other arrangements, or using disruptive distribution, business models or technologies, and other competitive actions, or benefitting from foreign subsidies, government aid or other advantages not available to Air Canada, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Dependence on technology – Air Canada relies heavily on technology to operate its business and any inadequacy, failure or security breach could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada relies heavily on technology, including to operate its business, increase its revenues and reduce its costs. Air Canada's technology systems include those relating to its websites, passenger sales and services, cargo services, airport customer services, flight operations, loyalty program, communications, distribution, and other business activities. Air Canada's websites and other technology systems must efficiently accommodate a high volume of traffic and must securely and effectively process and deliver information critical to Air Canada's business and operations. Air Canada's business also requires the secure collection, processing, storage and effective governance of sensitive data, including personal information of its passengers, Aeroplan Members, employees, business partners and others. The effective, reliable and secure operation of the networks and systems (including third party systems) on which sensitive information is stored, transmitted and processed is critical to Air Canada's business.

The technology systems Air Canada relies on also depend on the performance of its many suppliers and Air Canada has less direct oversight over their security ecosystem and practices. These suppliers' performance is in turn dependent upon their respective technology ecosystems. Technology systems may be vulnerable to a variety of sources of failures, interruption or misuse, including by reason of human error, third-party suppliers' acts or omissions, natural disasters, terrorist attacks, telecommunications failures, power failures, misuse, unauthorized or fraudulent users (including cyber-attacks, malware, ransomware, computer viruses and the like), and other operational and security issues.

Like other entities operating in today's digital business environment, we are subject to threats to the security of our networks, systems and data. There is a growing number of sophisticated actors, including hackers, organized criminals, state-sponsored actors and other parties, and information security attacks have continued to grow in complexity. The emergence of new technologies, such as artificial intelligence continues to grow these threats. The magnitude and frequency of information security breaches and their potential for damage has also continued to grow.

In light of the evolving nature and sophistication of information security threats, our information security systems and controls must continuously adapt and require regular monitoring to ensure effectiveness. Despite our efforts, given the complexity and scale of our business, network infrastructure, technology and IT supporting systems, there can be no assurance that our information security systems and controls will be effective. We have been the target of cybersecurity attacks in the past and expect that we will continue to be in the future.

Any technology system failure, degradation, interruption, misuse or fraudulent use, security breach, or failure to comply with applicable confidentiality, privacy, security or other related obligations, whether at Air Canada or a third party on which Air Canada or its suppliers rely, could adversely affect Air Canada, including by damaging its reputation and exposing Air Canada to litigation, claims for contract breach, fines, sanctions and/or remediation costs, any of which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Interruptions or disruptions in service – Interruptions or disruptions in service could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada's business is significantly dependent upon its ability to operate without interruption to or from a number of airports, including its main hubs at Toronto, Montréal, and Vancouver. Delays or disruptions in service may arise from a variety of factors, including the performance of airline industry participants on which Air Canada's operations are dependent (including airports, security, customs, air navigation and other participants or services), security issues, technology failures, breaches or other incidents, weather conditions, labour shortages or conflicts in respect of personnel not employed by Air Canada such as airport workers, baggage handlers, air traffic controllers, security personnel, immigration and customs personnel and others supporting airport-related operations, infectious diseases, public health restrictions or other factors beyond the control of Air Canada. Any of these could have a material adverse impact on Air Canada, its business, results from operations and financial condition.

Interruptions and disruptions in service may be caused by, and the demand and cost of air travel may also be adversely impacted by, environmental conditions (which are also being driven by climate change which may also increase the frequency, duration and intensity of severe weather events), volcanic eruptions floods or other natural phenomena, as well as those arising from anthropogenic sources. Such events, including on the ground and at altitude (including turbulence events), or impacting airports or destinations served or flight routes used by Air Canada may impact the viability or cost of flying to such destinations, cause interruptions and disruptions in service, increase Air Canada's costs or adversely impact demand for air travel, any of which could have a material adverse impact on Air Canada, its business, results from operations and financial condition.

Key supplies and suppliers – Air Canada's failure or inability to source certain goods and services from key suppliers, including on favourable terms and on a timely basis could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada is dependent upon its ability to source, on favourable terms and costs, and without disruption, sufficient quantities of goods and services of desirable quality, in a timely manner or within planned timeframes, required for Air Canada's business or operations, such as fuel, aircraft and related parts, catering, airport services (including customs and security services and infrastructure to support demand), de-icing services, airport slots, aircraft maintenance services, cargo handling services and facilities, and information technology systems and services. Like other airlines, we are dependent on the high quality and stable engineering design, manufacturing and maintenance of aircraft and related parts and other products we purchase, and issues that arise may cause these to be unavailable.

In certain cases, Air Canada may only be able to source goods and services from a limited number of suppliers (or from sole source suppliers) and the transition to new or alternative suppliers, which may be necessitated by reason of such suppliers increasing their rates or by their failure, refusal or inability to deliver or perform, may not be possible or may take a significant amount of time or require significant resources. A failure, refusal, delay or inability of a supplier to supply Air Canada with goods and services of desirable quality on terms and pricing and within timeframes acceptable to Air Canada may arise as a result of a wide range of causes, many of which are beyond Air Canada's control. Global supply chains continue to be impacted since the end of the COVID-19 pandemic, including by reason of labour shortages, access to raw materials, and transportation logistics, and these have and may continue to impact Air Canada and its suppliers.

Any failure or the inability of Air Canada to successfully source goods and services of desirable quality on terms and pricing and within the timeframes acceptable to Air Canada could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Labour costs and labour relations – Air Canada may not be able to maintain labour costs at appropriate levels or secure labour agreements that permit it to successfully pursue its strategic initiatives. There can be no assurance that collective bargaining agreements will be renewed without labour conflicts and/or disruptions.

Labour costs constitute one of Air Canada's largest operating cost items. There can be no assurance that Air Canada will be able to maintain such costs at levels that do not negatively affect its business, results from operations and financial condition. Most of Air Canada's employees are unionized. Air Canada is engaged in collective bargaining with the Air Line Pilots Association, the union representing its pilots. As agreements with other unions will expire over the next few years, bargaining is expected to commence with them as well. Any future agreements or outcomes of negotiations or arbitrations, including in relation to wages or other labour costs or work rules, may result in increased labour costs or other charges, or terms and conditions restricting or reducing Air Canada's ability to sustain its business objectives or pursue its strategic initiatives, which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

There can be no assurance that collective agreements will be further renewed, including on terms consistent with Air Canada's expectations or comparable to its competitors' labour agreements, without labour conflict or action or that there will not otherwise be any labour conflict or action that could also lead to a degradation, interruption or stoppage in Air Canada's service or otherwise adversely affect the ability of Air Canada to execute on its business plans or operate its business, either of which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

In respect of the unions for Canadian-based employees, strikes or lockouts may lawfully occur following the term and negotiations of the renewal of collective agreements once a number of pre-conditions prescribed by the Canada Labour Code have been satisfied.

Any labour disruption or work stoppage by any of the unionized work groups of Jazz or other airlines operating flights on behalf of Air Canada, or other key suppliers, or of other parties with which Air Canada conducts business or relies on could have a material adverse effect on Air Canada, its business, results from operations and financial condition. In addition, labour conflicts at Star Alliance® partners or involving the operations of key airports could result in lower demand for connecting traffic with Air Canada, which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Strategic, business, technology and other important initiatives – A delay or failure to identify and devise, invest in and implement certain important initiatives could have a material impact on Air Canada, its business, results from operations and financial condition.

In order to operate its business, achieve its goals and remain competitive, Air Canada continually seeks to identify and devise, invest in, implement and pursue strategic, business, technology and other important initiatives, including to source of aircraft, participate in the leisure or lower-cost market, enter into or expand joint venture arrangements, address climate change, enhance revenues, reduce costs, improve business processes, implement new technologies (including artificial intelligence), expand network and capacity, and initiatives seeking to improve and ensure a consistently high-quality customer service experience. Strategic initiatives, including their development and implementation, may be adversely impacted by a wide range of factors, many of which are beyond Air Canada's control. Such factors include the need to seek legal or regulatory approvals, the performance of third parties (including suppliers, their products and services), their integration into Air Canada's other activities and processes as well as the adoption and acceptance of these initiatives including by Air Canada's customers, suppliers and personnel. A delay or a failure to sufficiently and successfully identify and devise, invest in or implement any strategic or important initiative could adversely affect Air Canada's ability to operate its business, achieve its goals and remain competitive and could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Fuel costs – Significant fluctuations or increases in fuel prices could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Fuel costs constitute one of Air Canada's largest operating cost items. Fuel prices fluctuate widely depending on many factors, including international market conditions, geopolitical events, jet fuel supply and refining costs, carbon pricing, or other climate change related regulations, taxes, levies or other measures, and the Canada/U.S. dollar exchange rate. Air Canada cannot accurately predict the future price of fuel and it may not be able to sufficiently, or may not, hedge the risk associated with fluctuations in fuel prices. Due to the competitive nature of the airline industry, Air Canada may not be able to pass on increases in fuel prices to its customers by increasing its pricing. Significant fluctuations (including increases) in fuel prices could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Financial Leverage – Air Canada has a significant amount of financial indebtedness. Air Canada may also not be able to obtain sufficient funds in a timely manner and on acceptable terms to provide adequate liquidity and to finance necessary operating and capital expenditures.

Air Canada has a significant amount of financial indebtedness from fixed obligations, including substantial obligations under aircraft leases, aircraft purchases and other financings. While Air Canada actively seeks to manage its indebtedness, it may incur greater levels of indebtedness than currently exist or are planned.

The amount of indebtedness that Air Canada has and which it may incur in the future could have a material adverse effect on Air Canada. The ability of Air Canada to make scheduled payments under its indebtedness may depend on, among other things, its future operating performance and its ability to refinance its indebtedness, if necessary. Air Canada incurs a significant proportion of its indebtedness in foreign currencies, primarily in U.S. dollars, and as a result, future debt servicing repayments are subject to foreign exchange risk. There can be no assurance that Air Canada will at all times be able to generate sufficient cash from its operations to satisfy its debts, lease and other obligations and continue to pursue capital expenditures, and other business initiatives or strategic plans. Each of these factors is, to a large extent, subject to economic, financial, competitive, regulatory, operational and other factors, many of which are beyond Air Canada's control.

Need for capital and liquidity – Air Canada may not be able to obtain sufficient funds in a timely way and on acceptable terms to provide adequate liquidity and to finance necessary operating and capital expenditures.

Air Canada's liquidity levels may be adversely impacted by risks identified in this MD&A, including geopolitical, economic and public health conditions, foreign exchange rates, increased competition, volatile fuel prices, labour issues, and contractual covenants. As part of Air Canada's efforts to manage risk and to support its business strategy, significant liquidity and significant ongoing operating and capital expenditures are required.

Air Canada's level of indebtedness, as well as market conditions and the availability of assets as collateral for loans or other indebtedness, may make it difficult for Air Canada to raise additional capital if needed to meet its liquidity needs on acceptable terms, or at all.

A major decline in the market price of Air Canada's securities, including a major decline in capital markets in general, a downgrade in Air Canada's credit ratings, differences between Air Canada's actual or anticipated financial results and the published expectations of financial analysts, and differences between the estimated and available value of Air Canada's unencumbered assets, as well as events affecting its business or operating environment, may negatively impact Air Canada's ability to raise capital, issue debt, borrow on acceptable terms, attract and/or retain key employees, make strategic acquisitions, enter into business arrangements or operate its business.

There can be no assurance that Air Canada will continue to maintain sufficient liquidity, whether from operations or by obtaining funds on terms acceptable to Air Canada, to finance the operating and capital expenditures necessary to support its business strategy and manage any challenges.

Regional carrier service – The failure by a regional carrier to fulfill its obligations to Air Canada could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada enhances its network through agreements with certain airlines such as Jazz which operate flights on behalf of Air Canada. Pursuant to the terms of the Jazz CPA, Air Canada pays Jazz a number of fees, some of which are fixed and others that are determined based upon certain costs incurred by Jazz. Air Canada also reimburses Jazz for certain pass-through costs incurred by Jazz (or arranges to provide the related supplies to Jazz), such as fuel costs, navigation fees, landing fees and terminal fees. In addition, the Jazz CPA requires that Jazz maintain a minimum fleet size and contains a minimum average daily utilization guarantee, which requires Air Canada to use Jazz for that amount of flying. Significant increases in Jazz's costs, the failure by Jazz to adequately fulfill its obligations under the Jazz CPA, factors that may reduce the utilization of the Jazz fleet, including economic or market downturns, and unexpected interruptions or cessation of Jazz's services, as well as similar circumstances relating to other airlines from whom Air Canada may source regional capacity, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Personnel – Air Canada is dependent on key employees and having sufficient personnel and could be materially adversely affected by a shortfall or substantial turnover.

Air Canada is dependent on its ability to attract and retain a variety of employees, including senior leadership, managers, airline flight, technology and operations personnel and other key employees, including for specialized technical roles, having the necessary industry experience, qualifications and knowledge in order to execute its business plan and operate its business. If Air Canada were to experience a shortfall or a substantial turnover in its key employees (including as a result of the more competitive labour market), Air Canada, its business, results from operations and financial condition could be materially adversely affected.

Infectious diseases – Infectious diseases could impact passenger demand for air travel.

Outbreaks or the threat of outbreaks of viruses or other contagions or infectious diseases, including an epidemic or a pandemic such as COVID-19, influenza, SARS, Ebola, Zika, as well as any government actions, or travel or other advisories relating to same, whether domestic or international or whether relating to Canadian cities or regions or other cities, regions or countries, could have a material adverse effect on demand for air travel and could have a material adverse effect on Air Canada, its business, results from operations and financial condition. During the period from March 2020 until early- to mid-2022, Air Canada and the rest of the global airline industry faced significantly lower traffic than in 2019, and a corresponding decline in revenue and cash flows, as a result of the COVID- 19 pandemic and the travel restrictions imposed in many countries around the world including in Canada. Conditions have improved significantly, and travel restrictions have been lifted in many countries, including in Canada, however, there can be no assurance that there will not be further impacts or that the recovery will continue as expected, including as a result of further waves, supply chain disruptions and inflationary pressures.

Regulatory matters – Air Canada is subject to extensive and continually evolving domestic and international legal, regulatory and administrative controls and oversight.

Air Canada and the airline industry are subject to extensive and continually evolving domestic and international legal, regulatory and administrative controls and oversight, including in relation to taxes, charges, airport fees and operations, route rights, airport slots, aircraft operations and maintenance, security, air passenger and consumer protection rights, public health and safety, accessibility of transportation, flight crew and other labour rules, privacy, data security, marketing and advertising, licensing, competition, joint ventures, pensions, environment (including in relation to fuel management, pollution, climate change, greenhouse gas emissions and noise levels), customs, immigration, foreign exchange controls, repatriation of funds and, in some measure, pricing.

Air Canada is subject to significant and continually evolving tax laws, regulations and interpretations, which apply to its operations in various jurisdictions throughout the world. For example, a significant majority of countries in the Organisation for Economic Co-operation and Development's (OECD) Inclusive Framework approved a framework that imposes a global minimum tax rate of 15%. Canada introduced draft legislation to implement it and other jurisdictions that Air Canada operates to have also indicated their intent to introduce similar legislation. The OECD also continues to work on proposed changes to profit reallocation to market jurisdictions. Air Canada cannot predict whether, or the manner in which, proposed domestic and international laws (including in respect of the work of the OECD Inclusive Framework), regulations and administrative requirements or similar initiatives will ultimately be implemented or their impact on Air Canada.

Air Canada has and continues to establish targets, make commitments, and assess the impact regarding climate change, and related initiatives, plans and proposals that Air Canada and other stakeholders (including government, regulatory and other bodies) are pursuing in relation to climate change and carbon emissions. Air Canada has incurred, and expects to continue to incur, costs to achieve its goal of net zero carbon emissions and to comply with environmental sustainability legislation and regulation and other standards and accords. The precise nature of future binding or non-binding legislation, regulation, standards and accords, which is receiving increased focus of multiple stakeholders locally and internationally, cannot be predicted with any degree of certainty nor can their financial, operational or other impact. There can be no assurance of the extent to which any of our climate goals will be achieved or that any future investments that we make in furtherance of achieving our climate goals will produce the expected results or meet increasing stakeholder environmental, social and governance expectations. Moreover, future events could lead Air Canada to prioritize other nearer-term interests over progressing toward our current climate goals based on business strategy, economic, regulatory and social factors, business strategy or potential pressure from investors, activist groups or other stakeholders. If we are unable to meet or properly report on our progress toward achieving our climate change goals and commitments, we could face adverse publicity and reactions from other investors, customers, advocacy groups, or other stakeholders, which could result in reputational harm or other adverse effects to Air Canada.

While Air Canada seeks to comply with all applicable laws, regulations and administrative requirements, compliance may involve significant judgment in interpreting them. Furthermore, interpretations as well as the application and enforcement of such requirements may evolve due to numerous factors, including decisions by courts, regulators, administrative and other bodies. Compliance (including failure to comply) with current or future domestic and international laws, regulations and administrative requirements, including potentially inconsistent or conflicting laws or regulations, or laws or regulations that disproportionally apply to Canadian airlines or Air Canada specifically, may impose significant costs (including taxes, fines, penalties and/or levies), impediments and/or competitive disadvantages. There cannot be any assurance that current or future laws, regulations and administrative requirements will not materially adversely affect Air Canada, its business, results from operations and financial condition.

Terrorist attacks and security measures – Terrorist attacks and related consequences could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

The potential for terrorist attacks and terrorist activity causes concern and uncertainty in the minds of the travelling public. The occurrence of a terrorist attack, an attempted attack or the perceived threat of one (whether or not involving Air Canada or another carrier, or involving Air Canada's destinations, or other destinations or regions) and restrictive security measures, such as those relating to the content of carry-on baggage, passenger identification document requirements and passenger screening procedures, could have a material adverse effect on passenger demand for air travel and on the number of passengers travelling on Air Canada's flights. It could also lead to a substantial increase in insurance, security and other costs. Any resulting reduction in revenues and/or increases in costs could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Aeroplan loyalty program – Loss of redemption or accrual partners, changes to accrual or redemption settlement rates, increased redemption rates of loyalty points, or disruptions or other interruptions of services affecting the Aeroplan loyalty program could have a material adverse effect on Air Canada, its business, results from operations and financial condition

Air Canada offers its customers who are Aeroplan Members the opportunity to earn Aeroplan points, which management believes is a significant factor in many customers' decision to travel with Air Canada and contributes to building customer loyalty. The success of the Aeroplan program is dependent on attracting new and retaining current members and on maintaining sufficient accumulation and redemption partners. Increases in redemption rates for outstanding Aeroplan points, failures to adequately operate the Aeroplan program, reductions in the prevailing interchange rates in Canada, or interruptions or disruptions of Aeroplan program services, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Casualty losses – Air Canada's business makes it subject to large liability claims for serious personal injury or death arising out of accidents or disasters.

Due to the nature of its core business, Air Canada may be subject to liability claims arising out of accidents or disasters involving aircraft on which Air Canada's customers are travelling or involving aircraft of other carriers maintained or otherwise serviced by Air Canada or through third parties providing services to Air Canada, including claims for serious personal injury or death. Any such accident or disaster may significantly harm Air Canada's reputation for safety, which would have a material adverse effect on Air Canada, its business, results from operations and financial condition. There can be no assurance that Air Canada's insurance coverage will be sufficient to cover one or more large claims and any shortfall may be material.

Accidents and disasters may occur despite all appropriate measures being taken, and as a result of a variety of factors beyond Air Canada's control including acts of terrorism and sabotage, security breaches, equipment failures, human error, severe weather, lightning strikes and other natural phenomenon, bird strikes as well as the increasing prevalence of unmanned aerial vehicles.

Star Alliance and Joint Ventures – Departure of a key member from Star Alliance or the failure by a key member to meet its obligations, including under joint ventures arrangements, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

The strategic and commercial arrangements with Star Alliance and other airlines, including Lufthansa AG, United Airlines, Air China and Emirates, provide Air Canada with important benefits, including codesharing, efficient connections and transfers, reciprocal participation in frequent flyer programs and use of airport lounges from the other members. Should a key member leave Star Alliance or should a Star Alliance or other airlines fail to meet its obligations toward Air Canada, Air Canada, its business, results from operations and financial condition could be materially adversely affected.

Air Canada's brand – The failure to preserve or grow the value of Air Canada's brand could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada believes that its success is dependent on the value of its brand and on Air Canada's ability to preserve, grow and leverage that value. The Air Canada brand is recognized throughout the world, and Air Canada has received high ratings in external brand value studies, based in part on consumer perceptions on a variety of subjective qualities. Air Canada believes it has and continues to build an excellent reputation globally for the safety and quality of its services, and for the delivery of a consistently positive passenger experience. Air Canada's reputation and brand could be damaged if they are exposed to significant adverse publicity including through social media. Adverse publicity, whether justified or not, can rapidly spread through social or digital media. To the extent we are subject to, or unable to respond timely and appropriately to adverse publicity, our brand and reputation may be damaged. Any failure to preserve or grow Air Canada's brand, including by reason of the conduct of Air Canada or any of its business partners, suppliers or other third parties, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Legal proceedings – Air Canada may be subject to legal proceedings which could have a material adverse impact.

In the course of conducting its business, Air Canada is subject to various claims and litigation (including class action claims), including with respect to its contractual arrangements and current or future laws and regulations. Any future claims or litigation could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Foreign exchange – A significant deterioration of the Canadian dollar relative to the U.S. dollar could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada's financial results are sensitive to the fluctuating value of the Canadian dollar. Air Canada incurs significant expenses in U.S. dollars for items such as fuel, aircraft purchases, aircraft leasing and maintenance, airport charges, ground package costs, sales and distribution costs, interest and debt servicing payments, while a substantial portion of its revenues are generated in Canadian dollars. In addition, Air Canada may not be able to sufficiently, or may not, hedge the risk associated with fluctuations in exchange rates. A significant deterioration of the Canadian dollar relative to the U.S. dollar or other foreign currencies would increase the costs of Air Canada relative to its U.S. or other foreign competitors. Any of these factors could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Limitations due to restrictive covenants – Covenants in agreements that Air Canada has entered into or may enter into may affect or limit the manner in which Air Canada operates its business.

Some of the financing and other major agreements to which Air Canada is a party contain, and in the future may contain, restrictive, financial (including in relation to asset valuations, liquidity, fixed charge coverage ratio) and other covenants that affect and, in some cases, significantly limit or prohibit, among other things, the manner in which Air Canada may structure or operate its business, including by reducing Air Canada's liquidity, limiting Air Canada's ability to incur indebtedness, create liens, sell assets, pay dividends, make capital expenditures, and engage in acquisitions, mergers or restructurings or a change of control. Future financing and other significant agreements may be subject to similar or stricter covenants that limit Air Canada's operating and financial flexibility, which could materially and adversely affect Air Canada's ability to operate its business and its profitability.

A failure by Air Canada to comply with its contractual obligations (including restrictive, financial and other covenants) or to pay its indebtedness and fixed costs could result in a variety of material adverse consequences, including the acceleration of its indebtedness, the withholding of credit card proceeds by the credit card service providers and the exercise of remedies by its creditors, lessors or other co-contracting parties, including the foreclosure of Air Canada assets that secure obligations under secured financing agreements. Defaults could also trigger additional defaults under other indebtedness or agreements. In such a situation, Air Canada may not be able to repay the accelerated indebtedness or fulfill its obligations under certain contracts, make required aircraft lease payments or otherwise cover its fixed costs.

Availability of insurance coverage and increased insurance costs – Increases in insurance costs or reduction in insurance coverage could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

The insurance industry in general, including the aviation insurance industry, has been experiencing increasing losses and decreased insurer profitability in recent years, resulting in reduced capacity levels and premium increases. These conditions may adversely affect some of Air Canada's existing insurance carriers or Air Canada's ability to obtain future insurance coverage (including war risk insurance coverage), including desired levels of coverage or on terms acceptable to Air Canada. To the extent that Air Canada's existing insurance carriers are unable or unwilling to provide required coverage (and in the absence of measures by the Government of Canada to provide the required coverage), Air Canada's insurance costs may increase further and may result in Air Canada being in breach of regulatory requirements or contractual arrangements requiring that specific insurance be maintained, which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Pension plans – Failure or inability by Air Canada to make required cash contributions to its pension plans could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Air Canada maintains several defined benefit pension plans, including domestic registered pension plans and supplemental pension plans.

Canadian federal pension legislation requires that the funded status of defined benefit registered pension plans be determined periodically, on both a going concern basis (essentially assuming indefinite plan continuation) and a solvency basis (essentially assuming immediate plan termination). Canadian federal pension legislation prescribes the minimum contributions that plan sponsors must make to their defined benefit registered pension plans. Current service contributions are required to be paid monthly, except to the extent they are funded through the surplus in such plan (subject to applicable plan rules and legislation). Air Canada's pension funding obligations (including projected funding obligations) may vary significantly based on a wide variety of factors, including the plan's solvency financial position, regulatory developments, plan demographics, changes to plan provisions, the success of its pension asset investment strategies, assumptions and methods used and changes in economic conditions (mainly the return on fund assets and changes in interest rates) and other factors. Air Canada has taken significant steps to reduce its pension plan risk, and its domestic defined benefit registered pension plans are in a surplus position, but there can be no assurance that such a risk will not materialize and adversely impact Air Canada's ability to meet its funding obligations, which in turn could have a material adverse effect on Air Canada, its business, results from operations and financial condition. See section 8.6 "Pension Funding Obligations" of this MD&A for additional information.

19. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures and Internal Controls over Financial Reporting

Disclosure controls and procedures within Air Canada have been designed to provide reasonable assurance that all relevant information is identified to its President and Chief Executive Officer (CEO) and its Chief Financial Officer (CFO) and its Disclosure Policy Committee to ensure appropriate and timely decisions are made regarding public disclosure.

Internal controls over financial reporting have been designed by management, under the supervision of, and with the participation of Air Canada's CEO and CFO, to provide reasonable assurance regarding the reliability of Air Canada's financial reporting and its preparation of financial statements for external purposes in accordance with GAAP.

Air Canada will file certifications, signed by its CEO and CFO, with the Canadian Securities Administrators (CSA) upon filing of Air Canada's Annual Information Form. In those filings, Air Canada's CEO and CFO will certify, as required by National Instrument 52-109, the appropriateness of the financial disclosure, the design and effectiveness of Air Canada's disclosure controls and procedures and the design and effectiveness of internal controls over financial reporting. Air Canada's CEO and CFO also certify the appropriateness of the financial disclosures in Air Canada's interim filings with securities regulators. In those interim filings, Air Canada's CEO and CFO also certify the design of Air Canada's disclosure controls and procedures and the design of internal controls over financial reporting.

Air Canada's Audit, Finance and Risk Committee reviewed this MD&A and the audited consolidated financial statements, and Air Canada's Board of Directors approved these documents prior to their release.

Management's Report on Disclosure Controls and Procedures

Management, under the supervision of and with the participation of Air Canada's CEO and CFO, evaluated the effectiveness of Air Canada's disclosure controls and procedures (as defined under National Instrument 52-109) and concluded, as at December 31, 2023, that such disclosure controls and procedures were effective.

Management's Report on Internal Controls over Financial Reporting

Management, under the supervision of and with the participation of Air Canada's CEO and CFO, evaluated the effectiveness of Air Canada's internal controls over financial reporting (as defined under National Instrument 52-109). In making this evaluation, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commissions (COSO) in Internal Control - Integrated Framework (2013). Based on that evaluation, management and the CEO and CFO have concluded that, as at December 31, 2023, Air Canada's internal controls over financial reporting were effective. This evaluation took into consideration Air Canada's Corporate Disclosure Policy and the functioning of its Disclosure Policy Committee.

Changes in Internal Controls over Financial Reporting

There have been no changes to Air Canada's internal controls over financial reporting during 2023 that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

20. NON-GAAP FINANCIAL MEASURES

Below is a description of certain non-GAAP financial measures and ratios used by Air Canada to provide readers with additional information on its financial and operating performance. Such measures are not recognized measures for financial statement presentation under GAAP, do not have standardized meanings, may not be comparable to similar measures presented by other entities and should not be considered a substitute for or superior to GAAP results.

Adjusted CASM

Air Canada uses adjusted CASM to assess the operating and cost performance of its ongoing airline business without the effects of aircraft fuel expense, the cost of ground packages at Air Canada Vacations, impairment of assets and freighter costs as these items may distort the analysis of certain business trends and render comparative analysis across periods less meaningful and their exclusion generally allows for a more meaningful analysis of Air Canada's operating expense performance and a more meaningful comparison to that of other airlines.

In calculating adjusted CASM, aircraft fuel expense is excluded from operating expense results as it fluctuates widely depending on many factors, including international market conditions, geopolitical events, jet fuel refining costs and Canada/U.S. currency exchange rates. Air Canada also incurs expenses related to ground packages at Air Canada Vacations which some airlines, without comparable tour operator businesses, may not incur. In addition, these costs do not generate ASMs and therefore excluding these costs from operating expense results provides for a more meaningful comparison across periods when such costs may vary.

Air Canada also incurs expenses related to the operation of freighter aircraft which some airlines, without comparable cargo businesses, may not incur. Air Canada had seven Boeing 767 dedicated freighter aircraft in its operating fleet as at December 31, 2023, compared to three Boeing 767 dedicated freighter aircraft in service as at December 31, 2022. These costs do not generate ASMs and therefore excluding these costs from operating expense results provides for a more meaningful comparison of the passenger airline business across periods.

Adjusted CASM is reconciled to GAAP operating expense as follows:

(Canadian dollars in millions, except where indicated)	Fourth Quarter			Full Year		
	2023	2022	Change	2023	2022	Change
Operating expense – GAAP	**$ 5,096**	**$ 4,708**	**$ 388**	**$ 19,554**	**$ 16,743**	**$ 2,811**
Adjusted for:						
Aircraft fuel	(1,391)	(1,459)	68	(5,318)	(5,276)	(42)
Ground package costs	(177)	(163)	(14)	(720)	(474)	(246)
Impairment of assets	-	-	-	-	(4)	4
Freighter costs (excluding fuel)	(46)	(27)	(19)	(157)	(86)	(71)
Operating expense, adjusted for the above-noted items	**$ 3,482**	**$ 3,059**	**$ 423**	**13,359**	**10,903**	**2,456**
ASMs (millions)	**24,439**	**22,368**	**9.3%**	**99,012**	**82,558**	**19.9%**
Adjusted CASM (cents)	**¢ 14.25**	**¢ 13.68**	**¢ 0.57**	**¢ 13.49**	**¢ 13.21**	**¢ 0.28**

EBITDA and Adjusted EBITDA

EBITDA (earnings before interest, taxes, depreciation and amortization) is commonly used in the airline industry and is used by Air Canada as a means to view operating results before interest, taxes, depreciation and amortization as these costs can vary significantly among airlines due to differences in the way airlines finance their aircraft and other assets. In adjusted EBITDA, Air Canada excludes the effect of impairment of assets as it may distort the analysis of certain business trends and render comparative analysis across periods or to other airlines less meaningful.

Adjusted EBITDA Margin

Adjusted EBITDA margin (adjusted EBITDA as a percentage of operating revenues) is commonly used in the airline industry and is used by Air Canada as a means to measure the operating margin before interest, taxes, depreciation and amortization as these costs can vary significantly among airlines due to differences in the way airlines finance their aircraft and other assets. Further, the effects of impairment of assets are also removed in computing adjusted EBITDA margin as it may distort the analysis of certain business trends and render comparative analysis across periods or to other airlines less meaningful.

EBITDA, adjusted EBITDA and adjusted EBITDA margin are reconciled to GAAP operating income (loss) as follows:

	Fourth Quarter			Full Year		
(Canadian dollars in millions, except where indicated)	**2023**	**2022**	**Change**	**2023**	**2022**	**Change**
Operating income (loss) – GAAP	**$ 79**	**$ (28)**	**$ 107**	**$ 2,279**	**$ (187)**	**$ 2,466**
Add back:						
Depreciation and amortization	442	417	25	1,703	1,640	63
EBITDA	**$ 521**	**$ 389**	**$ 132**	**$ 3,982**	**$ 1,453**	**$ 2,529**
Remove:						
Impairment of assets	-	-	-	-	4	(4)
Adjusted EBITDA	**$ 521**	**$ 389**	**$ 132**	**$ 3,982**	**$ 1,457**	**$ 2,525**
Operating revenues	**$ 5,175**	**$ 4,680**	**$ 495**	**$ 21,833**	**$ 16,556**	**$ 5,277**
Operating margin (%)	**1.5**	**(0.6)**	**2.1 pp**	**10.4**	**(1.1)**	**11.5 pp**
Adjusted EBITDA margin (%)	**10.1**	**8.3**	**1.8 pp**	**18.2**	**8.8**	**9.4 pp**

Adjusted Pre-tax Income (Loss)

Adjusted pre-tax income (loss) is used by Air Canada to assess the overall pre-tax financial performance of its business without the effects of impairment of assets, foreign exchange gains or losses, net interest relating to employee benefits, gains or losses on financial instruments recorded at fair value, gains or losses on sale and leaseback of assets, gains or losses on disposal of assets, gains or losses on debt settlements and modifications, as these items may distort the analysis of certain business trends and render comparative analysis across periods or to other airlines less meaningful.

Adjusted pre-tax income (loss) is reconciled to GAAP income (loss) before income taxes as follows:

	Fourth Quarter			Full Year		
(Canadian dollars in millions)	**2023**	**2022**	**$ Change**	**2023**	**2022**	**$ Change**
Income (loss) before income taxes – GAAP	**$ 122**	**$ 146**	**$ (24)**	**$ 2,212**	**$ (1,524)**	**$ 3,736**
Adjusted for:						
Impairment of assets	-	-	-	-	4	(4)
Foreign exchange (gain) loss	(72)	(316)	244	(389)	732	(1,121)
Net interest relating to employee benefits	(7)	(7)	-	(25)	(24)	(1)
Gain on financial instruments recorded at fair value	(91)	(44)	(47)	(115)	(133)	18
Loss on debt settlements and modifications	1	31	(30)	10	14	(4)
Gain on disposal of assets	-	(21)	21	-	(21)	21
Adjusted pre-tax income (loss)	**$ (47)**	**$ (211)**	**$ 164**	**$ 1,693**	**$ (952)**	**$ 2,645**

Adjusted Net Income (loss) and Adjusted Earnings (Loss) per Share – Diluted

Air Canada uses adjusted net income (loss) and adjusted earnings (loss) per share – diluted as a means to assess the overall financial performance of its business without the after-tax effects of impairment of assets, foreign exchange gains or losses, net financing expense relating to employee benefits, gains or losses on financial instruments recorded at fair value, gains or losses on sale and leaseback of assets, gains or losses on debt settlements and modifications, gains or losses on disposal of assets as these items may distort the analysis of certain business trends and render comparative analysis to other airlines less meaningful.

Adjusted net income (loss) and adjusted earnings (loss) per share are reconciled to GAAP net income as follows:

	Fourth Quarter			Full Year		
(Canadian dollars in millions)	**2023**	**2022**	**$ Change**	**2023**	**2022**	**$ Change**
Net income (loss) – GAAP	**$ 184**	**$ 168**	**$ 16**	**$ 2,276**	**$ (1,700)**	**$ 3,976**
Adjusted for:						
Impairment of assets	-	-	-	-	4	(4)
Foreign exchange (gain) loss	(72)	(316)	244	(389)	732	(1,121)
Net interest relating to employee benefits	(7)	(7)	-	(25)	(24)	(1)
Gain on financial instruments recorded at fair value	(91)	(44)	(47)	(115)	(133)	18
Loss on debt settlements and modifications	1	31	(30)	10	14	(4)
Gain on disposal of assets	-	(21)	21	-	(21)	21
Income tax, including for the above reconciling items (1)	(59)	(28)	(31)	(44)	140	(184)
Adjusted net income (loss)	**$ (44)**	**$ (217)**	**$ 173**	**$ 1,713**	**$ (988)**	**$ 2,701**
Weighted average number of outstanding shares used in computing diluted income per share (in millions)	358	358	-	376	358	18
Adjusted earnings (loss) per share – diluted	**$ (0.12)**	**$ (0.61)**	**$ 0.49**	**$ 4.56**	**$ (2.76)**	**$ 7.32**

(1) In 2023, the deferred income tax expense recorded in other comprehensive income related to remeasurements on employee benefit liabilities is offset by a deferred income tax recovery which was recorded through Air Canada's consolidated statement of operations. This recovery is removed from adjusted net income for the year 2023. In comparison, a deferred income tax expense was removed from adjusted net loss for the year 2022.

The table below reflects the share amounts used in the computation of basic and diluted earnings per share on an adjusted earnings per share basis.

	Fourth Quarter		Full Year	
(In millions)	**2023**	**2022**	**2023**	**2022**
Weighted average number of shares outstanding – basic	**358**	**358**	**358**	**358**
Effect of dilution	-	-	18	-
Weighted average number of shares outstanding – diluted	**358**	**358**	**376**	**358**

Free Cash Flow

Air Canada uses free cash flow as an indicator of the financial strength and performance of its business, indicating the amount of cash Air Canada can generate from operations and after capital expenditures. Free cash flow is calculated as net cash flows from operating activities minus additions to property, equipment, and intangible assets, and is net of proceeds from sale and leaseback transactions. Refer to section 8.4 "Cash Flow Movements" of this MD&A for a reconciliation of this non-GAAP financial measure to the nearest measure under GAAP.

Net Debt

Net debt is a capital management measure and a key component of the capital managed by Air Canada and provides management with a measure of its net indebtedness. Refer to section 8.2 "Net Debt" of this MD&A for a reconciliation of this non-GAAP measure to the nearest measure under GAAP.

21. GLOSSARY

Adjusted CASM – Refers to operating expense per ASM that is adjusted to remove the effects of aircraft fuel expense, ground packages costs at Air Canada Vacations, impairment of assets and freighter costs. Adjusted CASM is a non-GAAP financial measure. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Adjusted EBITDA – Refers to earnings before interest, taxes, depreciation and amortization, excluding impairment of assets. Adjusted EBITDA is a non-GAAP financial measure. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Adjusted EBITDA margin – Refers to adjusted EBITDA as a percentage of operating revenue. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Adjusted net income (loss) – Refers to the consolidated net income (loss) of Air Canada, adjusted to remove the after-tax effects of impairment of assets, foreign exchange gains or losses, net interest relating to employee benefits, gains or losses on financial instruments recorded at fair value, gains or losses on the sale and leaseback of assets, gains or losses on debt settlements and modifications, and gains or losses on disposal of assets. Adjusted net income (loss) is a non-GAAP financial measure. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Adjusted pre-tax income (loss) – Refers to the consolidated income (loss) of Air Canada before income taxes and adjusted to remove the effects of impairment of assets, foreign exchange gains or losses, net interest relating to employee benefits, gains or losses on financial instruments recorded at fair value, gains or losses on the sale and leaseback of assets, gains or losses on debt settlements and modifications, and gains or losses on disposal of assets. Adjusted pre-tax income (loss) is a non-GAAP financial measure. Refer to section 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Aeroplan – Refers to Aeroplan Inc.

Atlantic – When used in reference to airline operations, refers to operations and revenues from flights that cross the Atlantic Ocean with origins and destinations principally in Europe, India, the Middle East and North Africa.

Available seat miles or ASMs – Refers to a measure of passenger capacity calculated by multiplying the total number of seats available for passengers by the miles flown.

Average stage length – Refers to the average mile per departure seat and is calculated by dividing total ASMs by total seats dispatched.

CASM – Refers to operating expense per ASM.

Domestic – When used in reference to airline operations, refers to operations and revenues from flights within Canada.

Free cash flow – Refers to net cash flows from operating activities minus additions to property, equipment, and intangible assets, and is net of proceeds from sale and leaseback transactions. Free cash flow is a non-GAAP financial measure. Refer to sections 8.4 "Cash Flow Movements" and 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Jazz – Refers to Jazz Aviation LP.

Leverage ratio – Also known as net debt to adjusted EBITDA ratio. Refers to the ratio of net debt to trailing 12-month adjusted EBITDA (calculated by dividing net debt by trailing 12-month adjusted EBITDA). Leverage ratio is a non-GAAP financial measure. Refer to sections 8.2 "Net Debt" and 20 "Non-GAAP Financial Measures" of this MD&A for additional information.

Net debt – Refers to total long-term debt liabilities (including current portion) less cash, cash equivalents. and short- and long-term investments. Refer to section 8.2 "Net Debt" of this MD&A for a reconciliation of this capital management measure to the nearest measure under GAAP.

Other – When used in reference to airline operations, refers to operations and revenues from flights with origins and destinations principally in Central and South America, the Caribbean and Mexico.

Pacific – When used in reference to airline operations, refers to operations and revenues from flights that cross the Pacific Ocean with origins and destinations principally in Asia and Australia.

Passenger load factor – Refers to a measure of passenger capacity utilization derived by expressing Revenue Passenger Miles as a percentage of ASMs.

Passenger revenue per available seat mile or PRASM – Refers to average passenger revenue per ASM.

Percentage point (pp) – Refers to a measure for the arithmetic difference of two percentages.

Revenue passenger carried – Refers to the International Air Transport Association's definition of passenger carried whereby passengers are counted on a flight number basis rather than by journey/itinerary or by leg.

Revenue passenger miles or RPMs – Refers to a measure of passenger traffic calculated by multiplying the total number of revenue passengers carried by the miles they are carried.

Seats dispatched – Refers to the number of seats on non-stop flights. A non-stop flight refers to a single takeoff and landing.

U.S. Transborder – When used in reference to airline operations, refers to operations and revenues from flights between Canada and the United States.

Yield – Refers to average passenger revenue per RPM.