AIR CANADA

News Release

Air Canada Reports Second Quarter 2018 Results

- Second quarter EBITDAR of $646 million and operating income of $226 million
- Record second quarter operating revenues of $4.333 billion
- Record unrestricted liquidity of $5.064 billion
- Leverage ratio of 2.1

MONTREAL, July 27, 2018 – Air Canada today reported second quarter 2018 EBITDAR[(1)] (earnings before interest, taxes, depreciation, amortization, impairment and aircraft rent) of $646 million compared to second quarter 2017 EBITDAR of $681 million. Air Canada reported operating income of $226 million compared to operating income of $292 million in the second quarter of 2017. The airline reported adjusted pre-tax income[(1)] of $163 million in the second quarter of 2018 compared to adjusted pre-tax income of $229 million in the prior year's quarter. On a GAAP basis, in the second quarter of 2018, Air Canada reported a loss before income taxes of $71 million, compared to income before income taxes of $314 million in the second quarter of 2017. The second quarter of 2018 included a loss on disposal of assets of $186 million and losses on foreign exchange of $25 million while the second quarter of 2017 included gains on foreign exchange of $68 million and a gain on sale and leaseback of assets of $26 million.

"I am pleased to report another solid quarter of revenue growth, cost containment and unrestricted liquidity, in the face of significantly higher fuel prices. Our record revenues this quarter demonstrate the appeal of Air Canada's brand and underscore the continuing strong demand for air travel in all of our main markets. I thank our 30,000 employees for their hard work and dedication in taking care of our customers, which was recognized this month when Air Canada was named the Best Airline in North America for the second consecutive year at the Skytrax World Airline Awards celebrated in the U.K. Winning the award for the seventh time in nine years is a testament to the sustained progress we have made, something which all our employees should be very proud of, as I am," said Calin Rovinescu, President and Chief Executive Officer of Air Canada.

"During the second quarter, passenger revenue climbed 10.4 per cent to a record $3.921 billion and we generated EBITDAR of $646 million. We reported a solid 2.7 per cent increase in passenger revenue per available seat mile (PRASM), primarily driven by a higher yield, and also delivered a 1.0 per cent decrease in adjusted cost per available seat mile. Our unrestricted liquidity totaled a record $5.064 billion at quarter-end. We achieved these results despite contending with a 31 per cent rise in jet fuel price per litre from a year ago, showing the strength of our business plan.

"We did, however, revise our 2018 guidance for certain key financial metrics given the rapid increase in fuel prices in the first half of 2018. Nevertheless, we believe that the impact is short-term, that our robust business will enable us to stay on track and, as a result, we continue to expect to achieve our longer-term targets that were communicated at our last Investor Day. We estimate that we will be able to mitigate approximately 75 per cent of the expected 2018 annual fuel price increase through fare increases, other commercial initiatives and our cost transformation program.

“Everywhere, our ongoing strategy was on full display this past quarter. We launched 25 new routes this summer, introduced Air Canada Signature Service for North American premium customers, began offering satellite Wi-Fi on our wide-body international fleet, and we were recognized as one of the top five brands to work for in Canada. We also completed a complex joint venture agreement begun four years ago with Air China, making Air Canada the first North American carrier to negotiate a joint venture with a Chinese airline. This gives us unrivalled access from North America to the fastest growing and soon-to-be largest aviation market in the world, said Mr. Rovinescu.

“The Skytrax Award shows that our customers appreciate our progress and are rewarding us with their loyalty, with our aircraft flying 83.1 per cent full on average during the quarter. I thank our customers for choosing to fly Air Canada and we are committed to giving them ever more reasons to keep doing so,” concluded Mr. Rovinescu.

Second Quarter Income Statement Highlights

In the second quarter of 2018, on capacity growth of 7.5 per cent, record system passenger revenues of $3.921 billion increased $371 million or 10.4 per cent from the second quarter of 2017. The increase in system passenger revenues was driven by traffic growth of 8.2 per cent and a yield improvement of 2.0 per cent, despite an increase in average stage length of 2.4 per cent which had the effect of reducing system yield by 1.4 percentage points. On a stage-length adjusted basis, system yield increased 3.4 per cent year-over-year.

In the business cabin, system passenger revenues increased $98 million or 13.7 per cent from the second quarter of 2017 on traffic and yield growth of 10.3 per cent and 3.1 per cent, respectively.

In the second quarter of 2018, operating expenses of $4.107 billion increased $489 million or 14 per cent from the same quarter in 2017, mainly driven by higher fuel prices year-over-year and by the increase in capacity.

Air Canada’s cost per available seat mile (CASM(1)) increased 5.6 per cent from the second quarter of 2017. The airline’s adjusted CASM decreased 1.0 per cent from the prior year’s quarter, better than the 0.5 per cent to 1.5 per cent increase projected in Air Canada’s news release dated April 30, 2018. Air Canada’s better than projected adjusted CASM performance was largely driven by the acceleration of aircraft lease extensions (mainly from the third quarter of 2018) which resulted in a decrease to maintenance provisions, the impact of cost reduction initiatives related to Air Canada’s cost transformation program, and other operating expense reductions.

Air Canada recorded adjusted net income(1) of $114 million or $0.41 per diluted share in the second quarter of 2018 compared to adjusted net income of $226 million or $0.82 per diluted share in second quarter of 2017. On a GAAP basis, the airline reported a second quarter 2018 net loss of $77 million or $0.28 per diluted share compared to second quarter 2017 net income of $311 million or $1.13 per diluted share. In the second quarter of 2018, Air Canada recorded a loss on disposal of assets of $186 million related to the expected sale of 25 Embraer aircraft and losses on foreign exchange of $25 million. In the second quarter of 2017, Air Canada recorded gains on foreign exchange of $68 million and a gain of $26 million on the sale and leaseback of two Boeing 787 aircraft.

Financial and Capital Management Highlights

At June 30, 2018, unrestricted liquidity (cash, short-term investments and undrawn lines of credit) amounted to $5.064 billion, the highest level in Air Canada's history (December 31, 2017 – $4.181 billion).

At June 30, 2018, adjusted net debt of $6.111 billion decreased $5 million from December 31, 2017. In the second quarter of 2018, an increase in long-term debt and finance lease balances of $889 million was largely offset by an increase in cash and short-term investment balances of $866 million and a decrease in capitalized operating lease balances of $28 million. At June 30, 2018, Air Canada's leverage ratio[(1)] was 2.1, unchanged from December 31, 2017.

Net cash flows from operating activities of $853 million in the second quarter of 2018 improved $24 million compared to the second quarter of 2017. Negative free cash flow[(1)] of $13 million in the second quarter of 2018 represented a decrease of $318 million from the second quarter of 2017 mainly due to Air Canada having received proceeds of $371 million from the sale and leaseback of aircraft in the second quarter of 2017 while no such sale and leasebacks were effected in the second quarter of 2018.

For the 12 months ended June 30, 2018, return on invested capital (ROIC[(1)]) was 13.7 per cent, significantly higher than Air Canada's weighted average cost of capital of 7.5 per cent.

2017 Investor Day Targets and Current Outlook

At its September 2017 Investor Day, Air Canada provided guidance on key financial metrics:

- Annual EBITDAR margin (EBITDAR as a percentage of operating revenue) of 17-20 per cent in 2018, 2019 and 2020**:**

  Air Canada now expects to achieve an annual EBITDAR margin of approximately 16 per cent for the full year 2018. This decrease in projected EBITDAR margin takes into account a significantly higher fuel price per litre than that assumed in Air Canada's Investor Day news release dated September 19, 2017. As additional mitigation measures take effect, including further pricing and productivity improvements and the airline's $250 million Cost Transformation Program due for completion in 2019, Air Canada is confident that its EBITDAR margin and ROIC will normalize by year-end and that it will realize its Investor Day targets post-2018.

  - Air Canada continues to expect to achieve an annual EBITDAR margin of 17-20 per cent in 2019 and 2020.

- Annual ROIC of 13-16 per cent in 2018, 2019 and 2020:

Air Canada now expects its annual ROIC to be approximately 12 per cent in 2018. This decrease in projected annual ROIC reflects Air Canada's expectation of a lower level of adjusted net income than that previously anticipated.

  - Air Canada continues to expect to achieve an annual ROIC of 13-16 per cent in 2019 and 2020.

- Cumulative free cash flow of $2.0 billion to $3.0 billion over the 2018-2020 period.

  - Air Canada continues to expect to achieve this target.

- A leverage ratio not exceeding 1.2 by the end of 2020 (measured by adjusted net debt over trailing 12-month EBITDAR):

  - Air Canada continues to expect to achieve this target.

Full Year 2018 Free Cash Flow

Air Canada now expects positive free cash flow in the range of $350 to $500 million in 2018, as opposed to the range of $250 million to $500 million projected in Air Canada's news release dated April 30, 2018. This change takes into account a significantly higher fuel price per litre than that previously assumed for the full year 2018 and now includes net proceeds of $296 million from the anticipated sale of 25 Embraer 190 aircraft which are expected in the third quarter of 2018. After the sale is completed, Air Canada will operate these aircraft under sale-leaseback agreements until they gradually exit the fleet between 2018 to 2020, in line with Air Canada's current fleet plans.

Third Quarter and Full Year 2018 Adjusted CASM

For the third quarter of 2018, Air Canada expects adjusted CASM (which excludes fuel expense, the cost of ground packages at Air Canada Vacations and special items) to increase 2.0 to 3.0 per cent when compared to the third quarter of 2017.

Air Canada continues to expect full year 2018 adjusted CASM to range between a decrease of 0.5 per cent to an increase of 1.0 per cent when compared to the full year 2017. Approximately 0.75 percentage points of this range are driven by non-recurring costs for branding initiatives and new uniforms, customer service and technology investments, accelerated depreciation and sale-leaseback rent expense for Embraer 190 aircraft, and 2018 start-up costs of approximately $10 million related to Air Canada's new loyalty program scheduled to launch in 2020.

Additional Guidance

For the full year 2018:

<u>Depreciation, Amortization and Impairment Expense</u>

Air Canada now expects depreciation, amortization and impairment expense to increase by approximately $125 million from the full year 2017, as opposed to the increase of $150 million projected in Air Canada's news release dated April 30, 2018, due to the expected sale of 25 Embraer 190 aircraft in the third quarter of 2018. As noted above, following the sale of these aircraft, Air Canada will operate them under sale-leaseback agreements and, as a result, the decrease in depreciation expense will largely be offset by an increase in aircraft rent expense.

Employee Benefits Expense

Air Canada continues to expect employee benefits expense to increase by approximately $75 million from the full year 2017.

Aircraft Maintenance Expense

Air Canada continues to expect aircraft maintenance expense to increase by approximately $90 million from the full year 2017.

2018 Outlook – Major Assumptions: Assumptions were made by Air Canada in preparing and making forward-looking statements. As part of its assumptions, Air Canada assumes continued relatively modest Canadian GDP growth for the third quarter and full year 2018. Air Canada also expects that the Canadian dollar will trade, on average, at C$1.32 per U.S. dollar in the third quarter and at C$1.30 per U.S. dollar for the full year 2018 and that the price of jet fuel will average 80 CAD cents per litre in the third quarter and 78 CAD cents per litre for the full year 2018.

The following table summarizes the above-mentioned outlook for the third quarter and the full year 2018 and related major assumptions:

		Full Year 2018
EBITDAR Margin		Approximately 16%
ROIC		Approximately 12%
Free Cash Flow		$350 - $500 million
	Third Quarter 2018 versus Third Quarter 2017	**Full Year 2018 versus Full Year 2017**
Adjusted CASM	Increase of 2.0% to 3.0%	Range between a decrease of 0.5% to an increase of 1.0%
Depreciation, Amortization and Impairment Expense		Increase by $125 million
Employee Benefits Expense		Increase by $75 million
Aircraft Maintenance Expense		Increase by $90 million
Major Assumptions	**Third Quarter 2018**	**Full Year 2018**
Canadian GDP	Relatively modest growth	Relatively modest growth
Canadian dollar per U.S. dollar	1.32	1.30
Jet fuel price – CAD cents per litre	80	78

The outlook provided constitutes forward-looking statements within the meaning of applicable securities laws and is based on a number of additional assumptions and subject to a number of risks. Please see section below entitled “Caution Regarding Forward-Looking Information”.

(1) Non-GAAP Measures

Below is a description of certain non-GAAP measures used by Air Canada in an effort 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. Readers are advised to review the section entitled Non-GAAP Financial Measures in Air Canada’s Second Quarter 2018 MD&A for a further discussion of such non-GAAP measures and a reconciliation of such measures to Canadian GAAP.

- Adjusted net income (loss) and adjusted earnings (loss) per share – diluted are used by Air Canada as a means to assess the overall financial performance of its business without the after-tax effects of foreign exchange gains or losses, net financing income (expense) relating to employee benefits, mark-to-market adjustments on derivatives and other financial instruments recorded at fair value, gain on sale and leaseback of assets, gains or losses on debt settlements and modifications, gains or losses on disposal of assets, and special items as these may distort the analysis of certain business trends and render comparative analysis to other airlines less meaningful. Starting as of and including the fourth quarter of 2017, adjusted net income (loss) is determined net of tax.

- 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 foreign exchange gains or losses, net financing income (expense) relating to employee benefits, mark-to-market adjustments on derivatives and other financial instruments recorded at fair value, gain on sale and leaseback of assets, gains or losses on debt settlements and modifications, gains or losses on disposal of assets, and special items. Air Canada uses adjusted pre-tax income (loss) to determine return on invested capital.

- EBITDAR is commonly used in the airline industry and is used by Air Canada as a means to view operating results before interest, taxes, depreciation, amortization, impairment and aircraft rent as these costs can vary significantly among airlines due to differences in the way airlines finance their aircraft and other assets. Air Canada excludes special items from EBITDAR as such items would distort the analysis of certain business trends and render comparative analysis to other airlines less meaningful.

- Adjusted CASM is used by Air Canada as a means to assess the operating and cost performance of its ongoing airline business without the effects of fuel expense, the cost of ground packages at Air Canada Vacations® and special items, as such expenses may distort the analysis of certain business trends and render comparative analysis to other airlines less meaningful. 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.

- "Leverage ratio" refers to adjusted net debt to trailing 12-month EBITDAR leverage ratio and is commonly used in the airline industry and is used by Air Canada as a means to measure financial leverage. Leverage ratio is calculated by dividing adjusted net debt by trailing 12-month EBITDAR (excluding special items). As mentioned above, Air Canada excludes special items from EBITDAR results (which are used to determine leverage ratio) as such items would distort the analysis of certain business trends and render comparative analysis to other airlines less meaningful.

- Free cash flow is commonly used in the airline industry and is used by Air Canada as an indicator of the financial strength and performance of its business, indicating the amount of cash Air Canada is able to 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-leaseback transactions.

- Return on invested capital (ROIC) is used by Air Canada as a means to assess the efficiency with which it allocates its capital to generate returns. Return is based on adjusted pre-tax income (or loss, as applicable), excluding interest expense and implicit interest on operating leases. Invested capital includes average year-over-year long-term debt, average year-over-year finance lease obligations, average year-over-year shareholders' equity, net of excess cash not required to run its core business operations, and the value of capitalized operating leases (the latter calculated by multiplying annualized aircraft rent by 7). Air Canada calculates invested capital based on a book value-based method of calculating ROIC, as described above. Refer to the definition of adjusted pre-tax income (loss) for a discussion as to why Air Canada uses adjusted pre-tax income (loss) to assess the overall pre-tax financial performance of its business.

Air Canada's Second Quarter 2018 Interim Unaudited Consolidated Financial Statements and Notes and its Second Quarter 2018 Management's Discussion and Analysis of Results of Operations and Financial Condition are available on Air Canada's website at aircanada.com, and will be filed on SEDAR at **www.sedar.com**.

For further information on Air Canada's public disclosure file, including Air Canada's Annual Information Form dated March 19, 2018, consult SEDAR at **www.sedar.com**.

Analyst Conference Call Advisory

Air Canada will host its quarterly analysts' call today, July 27, 2018 at 08:30 E.T. Calin Rovinescu, President and Chief Executive Officer, Michael Rousseau, Executive Vice President and Chief Financial Officer, and Benjamin Smith, President, Airlines and Chief Operating Officer, will be available for analysts' questions. Immediately following the analysts' Q&A session, Mr. Rousseau and Pierre Houle, Managing Director and Treasurer, will be available to answer questions from term loan B lenders and holders of Air Canada's bonds. Media and the public may access this call on a listen-in basis. Details are as follows:

Dial 416-340-2218 or 1-800-478-9326

Live audio webcast: **https://bell.media-server.com/m6/p/3o95v3mr**

INFORMATION

Investor Relations: (514) 422-7353

Internet: aircanada.com

AIR CANADA

HIGHLIGHTS

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

(Canadian dollars in millions, except where indicated)	Second quarter			First six months		
	2018	2017 (1)	$ Change	2018	2017 (1)	$ Change
Financial Performance Metrics						
Operating revenues	4,333	3,910	423	8,404	7,552	852
Operating income	226	292	(66)	212	262	(50)
Income (loss) before income taxes	(71)	314	(385)	(255)	301	(556)
Net income (loss)	(77)	311	(388)	(247)	298	(545)
Adjusted pre-tax income (2)	163	229	(66)	91	166	(75)
Adjusted net income (2)	114	226	(112)	62	163	(101)
Operating margin %	5.2%	7.5%	(2.3) pp	2.5%	3.5%	(1.0) pp
EBITDAR (excluding special items) (2)	646	681	(35)	1,043	1,047	(4)
EBITDAR margin (excluding special items) % (2)	14.9%	17.4%	(2.5) pp	12.4%	13.9%	(1.5) pp
Unrestricted liquidity (3)	5,064	4,493	571	5,064	4,493	571
Net cash flows from operating activities	853	829	24	1,964	1,856	108
Free cash flow (2)	(13)	305	(318)	180	775	(595)
Adjusted net debt (2)	6,111	6,393	(282)	6,111	6,393	(282)
Return on invested capital ("ROIC") % (2)	13.7%	15.7%	(2.0) pp	13.7%	15.7%	(2.0) pp
Leverage ratio (2)	2.1	2.4	(0.3)	2.1	2.4	(0.3)
Diluted earnings (loss) per share	($0.28)	$1.13	($1.41)	($0.91)	$1.07	($1.98)
Adjusted earnings per share – diluted (2)	$0.41	$0.82	($0.41)	$0.22	$0.59	($0.37)
Operating Statistics (4)			% Change			% Change
Revenue passenger miles ("RPM") (millions)	22,654	20,928	8.2	43,094	39,269	9.7
Available seat miles ("ASM") (millions)	27,269	25,357	7.5	52,131	48,251	8.0
Passenger load factor %	83.1%	82.5%	0.5 pp	82.7%	81.4%	1.3 pp
Passenger revenue per RPM ("Yield") (cents)	17.3	17.0	2.0	17.2	17.0	1.2
Passenger revenue per ASM ("PRASM") (cents)	14.4	14.0	2.7	14.2	13.8	2.8
Operating revenue per ASM (cents)	15.9	15.4	3.0	16.1	15.7	3.0
Operating expense per ASM ("CASM") (cents)	15.1	14.3	5.6	15.7	15.1	4.0
Adjusted CASM (cents) (2)	10.6	10.7	(1.0)	11.1	11.1	(0.3)
Average number of full-time equivalent ("FTE") employees (thousands) (5)	30.0	27.8	8.0	29.4	27.3	7.7
Aircraft in operating fleet at period-end	413	393	5.1	413	393	5.1
Average fleet utilization (hours per day)	10.1	10.3	(2.0)	10.1	10.1	(0.4)
Seats dispatched (thousands)	15,713	14,962	5.0	30,645	29,242	4.8
Aircraft frequencies (thousands)	145.2	141.2	2.9	281.7	275.5	2.3
Average stage length (miles) (6)	1,736	1,695	2.4	1,701	1,650	3.1
Fuel cost per litre (cents)	80.2	61.3	30.9	76.9	62.2	23.6
Fuel litres (thousands)	1,370,194	1,300,061	5.4	2,652,032	2,493,793	6.3
Revenue passengers carried (thousands) (7)	12,535	11,895	5.4	24,189	22,819	6.0

(1) Air Canada adopted accounting standard IFRS 15 - Revenue from Contracts with Customers effective January 1, 2018 with restatement of 2017 amounts. ROIC and leverage ratio as at June 30, 2017 have not been restated for the adoption of this new accounting standard. Refer to section 9 "Accounting Policies" of Air Canada's Second Quarter 2018 MD&A for additional information.

(2) Adjusted pre-tax income, adjusted net income, adjusted earnings per share – diluted, EBITDAR (earnings before interest, taxes, depreciation, amortization, impairment and aircraft rent), EBITDAR margin, leverage ratio, free cash flow, ROIC and adjusted CASM are each non-GAAP financial measures and adjusted net debt is an additional GAAP measure. Refer to sections 6 and 14 of Air Canada's Second Quarter 2018 MD&A for descriptions of Air Canada's non-GAAP financial measures and additional GAAP measures. As referenced in the table above, special items are excluded from Air Canada's reported EBITDAR calculations. Refer to section 4 of Air Canada's Second Quarter 2018 MD&A for information on the special items.

(3) Unrestricted liquidity refers to the sum of cash, cash equivalents, short-term investments and the amount of available credit under Air Canada's revolving credit facilities. At June 30, 2018, unrestricted liquidity was comprised of cash and short-term investments of $4,670 million and undrawn lines of credit of $394 million. At June 30, 2017, unrestricted liquidity was comprised of cash and short-term investments of $4,054 million and undrawn lines of credit of $439 million.

(4) Except for the reference to average number of FTE employees, operating statistics in this table include third party carriers (such as Jazz Aviation LP ("Jazz"), Sky Regional Airlines Inc. ("Sky Regional"), Air Georgian Limited ("Air Georgian") and Exploits Valley Air Services Ltd. ("EVAS")) operating under capacity purchase agreements with Air Canada.

(5) Reflects FTE employees at Air Canada. Excludes FTE employees at third party carriers (such as Jazz, Sky Regional, Air Georgian and EVAS) 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.