



Third Quarter 2022

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

October 28, 2022



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)	Third Quarter			First Nine Months		
	2022	2021	\$ Change	2022	2021	\$ Change
Financial Performance Metrics						
Operating revenues	5,322	2,103	3,219	11,876	3,669	8,207
Operating income (loss)	644	(364)	1,008	(159)	(2,546)	2,387
Loss before income taxes	(504)	(679)	175	(1,670)	(3,364)	1,694
Net loss	(508)	(640)	132	(1,868)	(3,109)	1,241
Adjusted pre-tax income (loss) ⁽¹⁾	446	(649)	1,095	(741)	(3,194)	2,453
Operating margin (%)	12.1	(17.3)	29.4 pp ⁽⁸⁾	(1.3)	(69.4)	68.1
EBITDA (excluding special items) ⁽¹⁾	1,057	(67)	1,124	1,068	(1,486)	2,554
EBITDA margin ⁽¹⁾ (%)	19.9	(3.2)	23.1 pp	9.0	(40.5)	49.5 pp
Total liquidity ⁽²⁾	10,236	14,504	(4,268)	10,236	14,504	(4,268)
Net cash flows from (used in) operating activities	290	305	(15)	1,721	(2,010)	3,731
Free cash flow ⁽¹⁾	(43)	156	(199)	476	(2,694)	3,170
Net debt ⁽¹⁾	7,829	7,117	712	7,829	7,117	712
Diluted loss per share	(1.42)	(1.79)	0.37	(5.22)	(8.97)	3.75
Operating Statistics⁽³⁾	2022	2021	Change %	2022	2021	Change %
Revenue passenger miles ("RPMs") (millions)	22,118	7,915	179.5	47,970	11,433	319.6
Available seat miles ("ASMs") (millions)	25,562	11,116	130.0	60,190	19,327	211.4
Passenger load factor %	86.5%	71.2%	15.3 pp	79.7%	59.2%	20.5 pp
Passenger revenue per RPM ("Yield") (cents)	21.8	20.7	5.4	21.2	21.5	(1.3)
Passenger revenue per ASM ("PRASM") (cents)	18.8	14.7	28.1	16.9	12.7	33.0
Operating revenue per ASM (cents)	20.8	18.9	10.0	19.7	19.0	3.9
Operating expense per ASM ("CASM") (cents)	18.3	22.2	(17.5)	20.0	32.2	(37.8)
Adjusted CASM (cents) ⁽¹⁾	11.6	18.7	(38.1)	13.0	28.1	(53.6)
Average number of full-time-equivalent ("FTE") employees (thousands) ⁽⁴⁾	31.8	21.3	49.7	29.6	18.0	64.5
Aircraft in operating fleet at period-end ⁽⁵⁾	344	337	2.1	344	337	2.1
Seats dispatched (thousands)	13,951	7,094	96.7	34,348	12,333	178.5
Aircraft frequencies (thousands)	99.6	57.4	73.6	250.6	103.8	141.4
Average stage length (miles) ⁽⁶⁾	1,832	1,565	17.1	1,752	1,567	11.8
Fuel cost per litre (cents)	131.8	72.9	80.7	128.4	69.2	85.5
Fuel litres (thousands)	1,227,669	648,515	89.3	2,972,219	1,316,563	125.8
Revenue passengers carried (thousands) ⁽⁷⁾	11,466	5,067	126.3	26,046	7,356	254.1

(1) Adjusted pre-tax income (loss), EBITDA (excluding special items) (earnings before interest, taxes, depreciation, and amortization), EBITDA margin, free cash flow, net debt and adjusted CASM are non-GAAP financial measures, non-GAAP ratios or supplemental 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 16 "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.

(2) 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 September 30, 2022, of \$10,236 million consisted of \$9,206 million in cash, cash equivalents, short and long-term investments and \$1,030 million available under undrawn credit facilities. As at September 30, 2021, total liquidity of \$14,504 million consisted of \$9,565 million in cash and cash equivalents, short and long-term investments, and \$4,939 million available under undrawn credit facilities. These amounts also include funds (\$231 million at September 30, 2022 and \$92 million at September 30, 2021) held in trust by Air Canada Vacations in accordance with regulatory requirements governing advance sales for tour operators. Refer to section 10 "Accounting Policies" for a description of

the change in presentation related to restricted cash effective as of the third quarter of 2022 and pursuant to which certain amounts have been reclassified to cash and cash equivalents with the 2021 comparative figures also reclassified.

- (3) 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.*
- (4) Reflects FTE employees at Air Canada and its subsidiaries. Excludes FTE employees at third party carriers operating under capacity purchase agreements with Air Canada. As of September 30, 2022, there were 32,166 employees based in Canada.*
- (5) The number of aircraft in Air Canada's operating fleet at September 30, 2022 and at September 30, 2021 include certain aircraft that were grounded due to the impact of the COVID-19 pandemic. As at September 30, 2022, four aircraft remained grounded pending return to service maintenance.*
- (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 third quarter of 2022. This MD&A should be read in conjunction with Air Canada's interim unaudited condensed consolidated financial statements and notes for the third quarter of 2022 dated October 28, 2022, as well as Air Canada's 2021 annual audited consolidated financial statements and notes and Air Canada's 2021 MD&A each dated February 18, 2022. 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 ("IASB"), 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 17 "Glossary" of this MD&A. Except as otherwise noted or where the context may otherwise require, this MD&A is current as of October 27, 2022.

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 Air Canada's 2021 MD&A and section 14 "Risk Factors" of this MD&A. Air Canada issued a news release dated October 28, 2022 reporting on its results for the third quarter 2022. This news release is available on Air Canada's website at aircanada.com and on SEDAR's website at www.sedar.com. For further information on Air Canada's public disclosures, including Air Canada's Annual Information Form, consult SEDAR at www.sedar.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.

During the period from March 2020 until early 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, but the wide-ranging impact of the COVID-19 pandemic and certain other factors have impeded Air Canada's and the global airline industry's restart efforts, particularly during the summer of 2022, and has also affected the ability of some of its participants, on which Air Canada's operations are dependent, to support the surge in traffic. Over the period from June to mid-July, this led to a meaningful increase in flight delays and cancellations, and other operational disruptions and challenges. Flight delays and cancellations started to decrease in August and there was a progressive increase in operational stability experienced in the second half of the third quarter of 2022, however, there can be no assurance that further significant disruptions will not reoccur.

Other factors that may cause results to differ materially from results indicated in forward-looking statements include the ongoing effects from the COVID-19 pandemic, economic and geopolitical conditions such as the military conflict between

Russia and Ukraine, Air Canada's ability to successfully achieve or sustain positive net profitability, industry and market conditions and the demand environment, Air Canada's ability to pay its indebtedness and maintain or increase liquidity, competition, Air Canada's dependence on technology, cybersecurity risks, energy prices, Air Canada's ability to successfully implement appropriate strategic and other important initiatives (including Air Canada's ability to manage operating costs), other epidemic diseases, terrorist acts, war, Air Canada's dependence on key suppliers (including government agencies and other stakeholders supporting airport and airline operations), Air Canada's ability to successfully operate its loyalty program, interruptions of service, Air Canada's ability to attract and retain required personnel, the availability and onboarding of Air Canada's workforce, casualty losses, changes in laws, regulatory developments or proceedings, climate change and environmental factors (including weather systems and other natural phenomena and factors arising from anthropogenic sources), Air Canada's dependence on regional and other carriers, Air Canada's ability to preserve and grow its brand, employee and labour relations and costs, Air Canada's dependence on Star Alliance® and joint ventures, pending and future litigation and actions by third parties, currency exchange, limitations due to restrictive covenants, insurance issues and costs, pension plans, as well as the factors identified in Air Canada's public disclosure file available at www.sedar.com and, in particular, those identified in section 18 "Risk Factors" in Air Canada's 2021 MD&A and section 14 "Risk Factors" of this MD&A. 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 2022. Air Canada also assumes that the Canadian dollar will trade, on average, at C\$1.30 per U.S. dollar for the full year 2022 and that the price of jet fuel will average C\$1.33 per litre for the full year 2022.

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. STRATEGY

Air Canada is evolving its business to better prepare for the future. As part of these efforts, Air Canada has introduced "Rise Higher", its newly articulated business imperatives, intended to elevate every aspect of its business. As it embarks on this next chapter, Air Canada will:

- 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 the business by expanding its international reach, and continually exploring new opportunities
- Elevate its customers, and support the creation of meaningful customer experiences and human connections by leveraging innovations in technology, loyalty and products
- Foster a collaborative workplace that respects diverse cultures and languages, while making impactful contributions to society

In pursuit of this goal, in 2022, Air Canada will build upon and leverage its numerous competitive advantages, including:

- Its talented people, and award-winning culture
- A widely recognized and powerful brand
- 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 customer experience enhanced by competitive products and services, including the fully transformed Aeroplan program
- Air Canada Rouge, a lower-cost leisure carrier
- A growing cargo offering
- New core technologies and other technological improvements
- Its commitment to sustainability

Additional information on Air Canada's strategy can be found in section 5 "Strategy" of Air Canada's 2021 MD&A.

4. OVERVIEW & THIRD QUARTER 2022 HIGHLIGHTS

Third Quarter 2022 Financial Summary

The following is an overview of Air Canada's results of operations and financial position for the third quarter 2022 compared to the third quarter 2021, with selected comparisons to the third quarter 2019, being the pre-pandemic comparison period.

- Operating revenues of \$5,322 million compared to third quarter operating revenues of \$2,103 million in 2021, an increase of \$3,219 million. Compared to the third quarter of 2019, operating revenues recovered to about 96%.
- Operating expenses of \$4,678 million versus operating expenses of \$2,467 million in the third quarter of 2021, an increase of \$2,211 million or 90% on an operated capacity increase of about 130%, and an 81% increase in fuel price.
- Operating income of \$644 million, with an operating margin of 12.1%, improved from an operating loss of \$364 million from the third quarter of 2021. This marks the first quarterly operating income since the pandemic began.
- EBITDA (excluding special items) of \$1,057 million, with an EBITDA margin of 19.9%, improved \$1,124 million from the third quarter of 2021. No special items were recorded in the third quarter of 2022 whereas a total operating expense reduction of \$103 million was recorded as special items in the third quarter of 2021.
- Net cash flows from operating activities of \$290 million decreased \$15 million from the third quarter of 2021. Refer to section 7.5 "Cash Flow Movements" of this MD&A for additional information.
- In September 2022, Air Canada repurchased \$273 million (US\$207 million) aggregate principal amount of its outstanding 4.000% Convertible Senior Notes due 2025 for an aggregate cash repurchase price of approximately \$329 million (US\$249 million), including accrued interest. Following this, \$747 million (US\$540 million) aggregate principal amount of Notes remains outstanding.

Travel Restrictions

During the first half of 2022, most of the remaining travel restrictions for fully vaccinated travellers were lifted by the Canadian government, and effective October 1, 2022, all remaining Government of Canada COVID-19 travel health restrictions and measures were lifted, including requirements for wearing masks on aircraft, testing and quarantine, and the compulsory use of the ArriveCan declaration application.

5. RESULTS OF OPERATIONS

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

(Canadian dollars in millions, except where indicated)	Third Quarter				First Nine Months			
	2022	2021	\$ Change	% Change	2022	2021	\$ Change	% Change
Operating revenues								
Passenger	\$ 4,818	\$ 1,636	\$ 3,182	194	\$ 10,176	\$ 2,457	\$ 7,719	314
Cargo	281	366	(85)	(23)	978	1,005	(27)	(3)
Other	223	101	122	121	722	207	515	249
Total operating revenues	5,322	2,103	3,219	153	11,876	3,669	8,207	224
Operating expenses								
Aircraft fuel	1,617	472	1,145	243	3,817	911	2,906	319
Wages, salaries, and benefits	816	592	224	38	2,272	1,617	655	41
Regional airlines expense, excluding fuel	400	312	88	28	1,083	700	383	55
Depreciation and amortization	413	400	13	3	1,223	1,217	6	0
Aircraft maintenance	193	153	40	26	414	430	(16)	(4)
Airport and navigation fees	299	166	133	80	723	373	350	94
Sales and distribution costs	217	74	143	193	496	142	354	249
Ground package costs	80	23	57	248	311	29	282	972
Catering and onboard services	120	52	68	131	278	94	184	196
Communications and information technology	112	85	27	32	331	271	60	22
Special items	-	(103)	103	(100)	4	(157)	161	(103)
Other	411	241	170	71	1,083	588	495	84
Total operating expenses	4,678	2,467	2,211	90	12,035	6,215	5,820	94
Operating income (loss)	644	(364)	1,008		(159)	(2,546)	2,387	
Non-operating income (expense)								
Foreign exchange loss	(951)	(136)	(815)		(1,048)	(74)	(974)	
Interest income	46	17	29		97	54	43	
Interest expense	(239)	(197)	(42)		(664)	(538)	(126)	
Interest capitalized	3	4	(1)		8	13	(5)	
Net interest relating to employee benefits	9	(1)	10		17	(10)	27	
Gain (loss) on financial instruments recorded at fair value	(25)	114	(139)		89	(114)	203	
Gain (loss) on debt settlements and modifications	17	(110)	127		17	(129)	146	
Other	(8)	(6)	(2)		(27)	(20)	(7)	
Total non-operating expense	(1,148)	(315)	(833)		(1,511)	(818)	(693)	
Loss before income taxes	(504)	(679)	175		(1,670)	(3,364)	1,694	
Income tax recovery (expense)	(4)	39	(43)		(198)	255	(453)	
Net loss	\$ (508)	\$ (640)	\$ 132		\$ (1,868)	\$ (3,109)	\$ 1,241	
Diluted loss per share	\$ (1.42)	\$ (1.79)	\$ 0.37		\$ (5.22)	\$ (8.97)	\$ 3.75	
EBITDA (excl. special items) ⁽¹⁾	\$ 1,057	\$ (67)	\$ 1,124		\$ 1,068	\$ (1,486)	\$ 2,554	
Adjusted pre-tax income (loss) ⁽¹⁾	\$ 446	\$ (649)	\$ 1,095		\$ (741)	\$ (3,194)	\$ 2,453	

(1) EBITDA (excluding special items) and adjusted pre-tax income (loss) are non-GAAP financial measures. Refer to section 16 "Non-GAAP Financial Measures" of this MD&A for additional information.

System Passenger Revenues

In the third quarter of 2022, passenger revenues of \$4,818 million increased \$3,182 million or almost three times from the third quarter of 2021. In the third quarter of 2022, traffic and total operated capacity more than doubled year-over-year, resulting in a 15-percentage point increase in passenger load factor compared to the same quarter in 2021. While operating conditions had begun to improve in the third quarter of 2021 as a result of the gradual lifting of certain travel restrictions imposed by the Government of Canada, the COVID-19 pandemic-related travel restrictions in place at that time continued to impact demand for travel, most notably to international destinations through the back half of 2021. In addition, in the first half of 2021, travel demand during this period was primarily for essential purposes, booked close to departure date and on shorter stage-length journeys than prior to the pandemic. Certain comparisons versus 2021 may not be meaningful due to the demand environment in 2021, primarily in the first six months. Air Canada believes that a comparison to the same periods of 2019 allows for a better understanding of passenger revenues and the development of Air Canada's recovery.

Third quarter 2022 passenger revenues were 94% of those in the third quarter of 2019, despite an operated capacity that represented 79% of the same period in 2019. Passenger load factor in the quarter was essentially unchanged compared to the third quarter of 2019, while PRASM and yield increased 19% and 18%, respectively. The capacity operated in the third quarter of 2022, was in line with the projection provided in Air Canada's news release dated August 2, 2022.

In the third quarter of 2022, at the cabin level, passenger revenues increased over three times for business, about four times for premium economy, and almost three times for economy, when compared to the third quarter of 2021. When compared to the third quarter of 2019, passenger revenues increased about 11% for the premium cabins, and economy cabin revenues reached about 89% of 2019 levels.

In addition to the subsequent discussion by service, the following factors contributed to the strong yield performance in the third quarter of 2022 versus the same period in 2019:

- Better fare mix in premium and economy cabins
- Higher average fare levels
- Yield upside from Aeroplan redemption bookings
- Changes in demand from local and connecting traffic

While third quarter 2022 yields increased when compared to the same period in 2021 and in 2019, the variances are also impacted by changes in average stage length. At the system level, average fares increased about 20% from the third quarter of 2019. Given the demand pattern for long-haul services in North America, the increase in average stage length negatively impacted yield gains. Average stage length, however, decreased for international services, when compared to the third quarter of 2019, which favourably impacted yields.

These results were driven by the continuation of the strong recovery in demand for air travel following the further easing of travel restrictions in Canada and in many countries Air Canada operates to, despite stringent restrictions in certain Pacific destinations.

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

(Canadian dollars in millions)	Third Quarter						
	2022	2021	\$ Change	% Change	2019	\$ Change	% Change
Canada	\$ 1,466	\$ 771	\$ 695	90	\$ 1,545	\$ (79)	(5)
U.S. transborder	915	291	624	215	995	(80)	(8)
Atlantic	1,770	384	1,386	361	1,613	157	10
Pacific	382	112	270	240	739	(357)	(48)
Other	285	78	207	264	249	36	14
System	\$ 4,818	\$ 1,636	\$ 3,182	195	\$ 5,141	\$ (323)	(6)

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

	Third Quarter 2022 versus Third Quarter 2021					
	Passenger Revenue % Change	Capacity (ASMs) % Change	Traffic (RPMs) % Change	Passenger Load Factor pp Change	Yield % Change	PRASM % Change
Canada	90	41	57	8	21	35
U.S. transborder	215	219	267	11	(14)	(1)
Atlantic	361	201	278	18	22	53
Pacific	240	111	265	37	(7)	61
Other	264	202	266	15	(0)	21
System	195	130	179	15	5	28

	Third Quarter 2022 versus Third Quarter 2019					
	Passenger Revenue % Change	Capacity (ASMs) % Change	Traffic (RPMs) % Change	Passenger Load Factor pp Change	Yield % Change	PRASM % Change
Canada	(5)	(15)	(15)	0	12	12
U.S. transborder	(8)	(11)	(11)	(0)	3	3
Atlantic	10	(9)	(8)	1	19	21
Pacific	(48)	(63)	(63)	1	40	41
Other	14	(10)	(12)	(2)	31	28
System	(6)	(21)	(21)	0	18	19

Domestic Passenger Revenues

In the third quarter of 2022, Domestic passenger revenues of \$1,466 million increased \$695 million or 90% from the third quarter of 2021. On a year-over-year capacity increase of 41%, traffic increased 57%, resulting in an eight-percentage-point increase in passenger load factor. These results largely reflect the increased demand for air services and greater availability of routes and frequencies across our domestic network. In 2021, as a result of the COVID-19 pandemic and

travel restrictions in place at that time, travel demand, most notably in the first half of 2021, was primarily for essential purposes, booked close-in to departure date and on shorter stage-length journeys than prior to the pandemic. This non-comparable environment, in 2021, generated statistically high yields.

Third quarter 2022 Domestic passenger revenues were 95% of those in the same period in 2019, on an operated capacity representing 85% of the third quarter of 2019. With an unchanged passenger load factor, PRASM and yield increased 12% each. These results are largely explained by the continued strength in demand and pricing for domestic passenger services and also reflect changes in travel mix with premium cabins outperforming the economy cabin. In addition, Domestic average fares increased about 21% from 2019 and average stage length also increased as a result of higher demand for our long-haul service.

In the first nine months of 2022, Domestic passenger revenues of \$3,229 million increased \$1,953 million or about two-and-a-half times from the same period in 2021 largely attributable to the impact of the COVID-19 pandemic and the significant travel restrictions in place in 2021, most notably in the first six months of 2021. Domestic passenger revenues were 81% of those in the first nine months of 2019 on an operated capacity that represented 81% of Domestic capacity in the first nine months of 2019.

U.S. Transborder Passenger Revenues

In the third quarter of 2022, U.S. transborder passenger revenues of \$915 million increased \$624 million or 215% from the third quarter of 2021. Year-over-year, traffic and capacity increased about 3.7 times and 3.2 times, respectively, resulting in an 11-percentage-point increase in passenger load factor. These results reflect the increased demand for air services and greater availability of routes and frequencies across our U.S. transborder network. In 2021, as a result of the COVID-19 pandemic and travel restrictions in place at that time, travel demand, most notably in the first half of 2021, was primarily for essential purposes, booked close-in to departure date and on shorter stage-length journeys than prior to the pandemic. This non-comparable environment, in 2021, generated statistically high yields.

Third quarter 2022 U.S. transborder passenger revenues were 92% of those in the same period in 2019, on an operated capacity representing 89% of that in the same quarter of 2019. Passenger load factor remained substantially equal when compared to the third quarter of 2019 while PRASM and yield increased 3% each, with gains in nearly all markets served. These results reflect strong demand and pricing for our U.S. transborder services as well as changes in traffic mix. Similar to our Domestic service, demand was strong on U.S. long-haul services and to U.S. leisure destinations. As such, the yield increase versus 2019 was negatively impacted by an increase in average stage length, however, average fares increased 14% from the same period in 2019.

In the first nine months of 2022, U.S. transborder passenger revenues of \$2,101 million increased \$1,749 million or about six times from the same period in 2021 largely attributable to the impact of the COVID-19 pandemic and the significant travel restrictions in place in 2021, most notably in the first six months of 2021. U.S. transborder passenger revenues were 73% of those in the first nine months of 2019, on an operated capacity that represented 74% of the capacity in the same period in 2019.

Atlantic Passenger Revenues

In the third quarter of 2022, Atlantic passenger revenues of \$1,770 million increased \$1,386 million or about 4.6 times from the third quarter of 2021. Year-over-year, capacity and traffic increased three times and about 3.8 times resulting in a 22-percentage-point increase in passenger load factor. In addition, PRASM and yield increased 53% and 22% respectively from the third quarter of 2021, with gains in almost all Atlantic markets served. These results reflect the increased demand for air services, in all cabins, and greater availability of routes and frequencies across our Atlantic network derived from a more normalized network and the return to a normalized demand environment following the easing of travel restrictions.

Third quarter 2022 Atlantic passenger revenues increased 10% from the third quarter of 2019, on an operated capacity of 91% of third quarter 2019 levels. Passenger load factor increased one percentage point while PRASM and yield increased 21% and 19%, respectively. These results reflect the strong demand for Atlantic destinations, in all cabins, all points of sale, including a strong return of 6th freedom traffic following the easing of travel restrictions.

In the first nine months of 2022, Atlantic passenger revenues of \$3,285 million increased \$2,739 million or about six times from the same period in 2021 largely attributable to the impact of the COVID-19 pandemic and the significant travel

restrictions in place in 2021, most notably in the first six months of 2021. Atlantic passenger revenues were 93% of those in the first nine months of 2019, on an operated capacity that represented 85% of the capacity in the same period in 2019.

Pacific Passenger Revenues

In the third quarter of 2022, Pacific passenger revenues of \$382 million increased \$270 million or about 3.4 times from the third quarter of 2021. Traffic increased 3.7 times while capacity doubled from the same period in 2021, resulting in a 37-percentage-point increase in passenger load factor. These results reflect a slightly better operating environment in certain destinations in the Pacific market following the very limited easing of certain travel restrictions, including with Hong Kong lifting the mandatory hotel quarantine effective September 26, 2022.

Third quarter 2022 Pacific passenger revenues were 52% of those in the third quarter of 2019 on a capacity that represented about a third of that operated in the same period of 2019 due to the significantly reduced capacity in all Pacific markets, most notably China and Hong Kong, as a result of the COVID-19-related travel restrictions that remained in place. Despite certain restrictions remaining in place, PRASM and yield increased 41% and 40%, respectively, compared to the third quarter of 2019.

In the first nine months of 2022, Pacific passenger revenues of \$706 million increased \$543 million or over four times from the first nine months of 2021 reflecting a slightly better operating environment in the Pacific market when compared to the same period in 2021. Pacific passenger revenues were 37% of those in the first nine months of 2019 while capacity represented 27% of that in the same period of 2019.

Other Passenger Revenues

In the third quarter of 2022, Other passenger revenues of \$285 million increased \$207 million or about 3.6 times from the same period in 2021. Year-over-year traffic and capacity increased 3.7 times and three times from the third quarter of 2021, respectively, resulting in a 15-percentage-point passenger load factor increase. These results reflect the increased demand for air services, in all cabins, and greater availability of routes and frequencies across our Caribbean, Central and South American network derived from a more normalized operating environment following the easing of travel restrictions.

Third quarter 2022 Other passenger revenues increased 14% from the third quarter of 2019 on an operated capacity that represented 90% of that in the same period of 2019. Yield and PRASM increased 31% and 28%, respectively, with gains in all markets served. These results reflect the strong demand, in all cabins, for Caribbean, Central and South American destinations derived from a robust demand recovery following the easing of travel restrictions.

In the first nine months of 2022, Other passenger revenues of \$855 million increased \$735 million or about seven times from the same period in 2021 reflecting a better operating environment in the Caribbean, Central and South American market when compared to the same period in 2021. Other passenger revenues were 88% of those in the first nine months of 2019 while capacity represented 79% of that in the same period of 2019.

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

(Canadian dollars in millions)	First Nine Months						
	2022	2021	\$ Change	% Change	2019	\$ Change	% Change
Canada	\$ 3,229	\$ 1,276	\$ 1,953	153	\$ 3,975	\$ (746)	(19)
U.S. transborder	2,101	352	1,749	498	2,892	(791)	(27)
Atlantic	3,285	546	2,739	502	3,526	(241)	(7)
Pacific	706	163	543	333	1,894	(1,188)	(63)
Other	855	120	735	610	970	(115)	(12)
System	\$ 10,176	\$ 2,457	\$ 7,719	314	\$ 13,257	\$ (3,081)	(23)

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

	First Nine Months of 2022 versus First Nine Months of 2021					
	Passenger Revenue % Change	Capacity (ASMs) % Change	Traffic (RPMs) % Change	Passenger Load Factor pp Change	Yield % Change	PRASM % Change
Canada	153	90	140	16	6	33
U.S. transborder	498	500	612	12	(16)	(0)
Atlantic	502	251	402	25	20	72
Pacific	333	141	366	39	(7)	80
Other	610	533	664	13	(7)	12
System	314	211	320	21	(1)	33

	First Nine Months of 2022 versus First Nine Months of 2019					
	Passenger Revenue % Change	Capacity (ASMs) % Change	Traffic (RPMs) % Change	Passenger Load Factor pp Change	Yield % Change	PRASM % Change
Canada	(19)	(19)	(23)	(3)	5	1
U.S. transborder	(27)	(26)	(32)	(6)	7	(2)
Atlantic	(7)	(15)	(18)	(2)	13	10
Pacific	(63)	(73)	(75)	(5)	48	39
Other	(12)	(21)	(30)	(10)	27	12
System	(23)	(30)	(34)	(4)	16	10

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

(millions)	Third Quarter				First Nine Months			
	2022		2021		2022		2021	
	RPMs	ASMs	RPMs	ASMs	RPMs	ASMs	RPMs	ASMs
Canada	5,349	6,325	3,417	4,483	12,103	15,189	5,050	7,991
U.S. transborder	3,569	4,260	973	1,336	8,286	10,934	1,163	1,824
Atlantic	9,735	10,971	2,576	3,647	18,961	22,962	3,776	6,541
Pacific	1,976	2,275	542	1,076	3,764	4,719	808	1,961
Other	1,489	1,731	407	574	4,856	6,386	636	1,010
System	22,118	25,562	7,915	11,116	47,970	60,190	11,433	19,327

Cargo Revenues

In the third quarter of 2022, Cargo revenues of \$281 million declined \$85 million or 23% from the third quarter of 2021, an increase of \$104 million or 59% when compared to the third quarter of 2019. The year-over-year decline was primarily due to lower year-over-year traffic in the Pacific market due to reduced freighter activities due the temporarily converted passenger aircraft no longer flying cargo-only flights and, to a lesser extent, to yield normalization, mainly in the U.S. transborder and Atlantic markets. The decline was partially offset by increased capacity and higher traffic in the Atlantic, U.S. transborder and Other markets.

In the first nine months of 2022, Cargo revenues of \$978 million declined \$27 million or about 3% from the same period in 2021, an increase of \$447 million or 84% when compared to the first nine months of 2019. The decline versus 2021 was mainly due to lower traffic in the Pacific markets and lower yield in the U.S. transborder and Atlantic markets and was partially offset by higher yields in the Pacific markets and higher traffic most notably in Other and Atlantic markets. These results largely reflect the impact of Air Canada no longer operating cargo-only flights using the temporarily converted passenger aircraft as of the end of the second quarter of 2022.

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

(Canadian dollars in millions)	Third Quarter				First Nine Months			
	2022	2021	\$ Change	% Change	2022	2021	\$ Change	% Change
Canada	\$ 26	\$ 30	\$ (4)	(12)	\$ 84	\$ 79	\$ 5	7
U.S. transborder	15	16	(1)	(11)	38	44	(6)	(15)
Atlantic	141	124	17	14	411	387	24	6
Pacific	70	168	(98)	(58)	343	426	(83)	(20)
Other	29	28	1	6	102	69	33	49
System	\$ 281	\$ 366	\$ (85)	(23)	\$ 978	\$ 1,005	\$ (27)	(3)

(Canadian dollars in millions)	Third Quarter				First Nine Months			
	2022	2019	\$ Change	% Change	2022	2019	\$ Change	% Change
Canada	\$ 26	\$ 31	\$ (5)	(14)	\$ 84	\$ 86	\$ (2)	(2)
U.S. transborder	15	12	3	8	38	37	1	0.3
Atlantic	141	61	80	130	411	189	222	117
Pacific	70	60	10	19	343	177	166	95
Other	29	13	16	120	102	42	60	141
System	\$ 281	\$ 177	\$ 104	59	\$ 978	\$ 531	\$ 447	84

Other Revenues

Other revenues of \$223 million in the third quarter of 2022 increased \$122 million or more than double from the third quarter of 2021 (\$72 million) and \$515 million in the first nine months of 2022, an increase of \$515 million or 3.5 times from the same period in 2021. The increases were primarily due to a higher volume of ground package revenues at Air Canada Vacations compared to the same periods in 2021, reflecting the increased demand for vacation packages and the impact of the suspension of flights to Mexico and the Caribbean between January 31, 2021 and June 26, 2021. To a lesser extent, higher onboard and Maple Leaf Lounge revenues driven by the return of traffic, higher non-air revenues related to the Aeroplan program, and higher passenger-related fees also contributed to the increases.

Operating Expenses

In the third quarter of 2022, total operating expense of \$4,678 million increased \$2,211 million or 90% from the third quarter of 2021. In the first nine months of 2022, total operating expenses of \$12,035 million increased \$5,820 million or 94% from the same period in 2021. The variances are primarily explained by increases in all line items largely reflecting the year-over-year growth in traffic and operated capacity. In addition, the significant increase in fuel price also contributed to the variance.

Aircraft Fuel

In the third quarter of 2022, fuel expense of \$1,617 million increased \$1,145 million or about three-and-a-half times from the third quarter of 2021. The increase was the result of jet fuel prices increasing about 81% year-over-year and to the higher volume of flying compared to the third quarter of 2021. To a lesser extent, an unfavourable foreign exchange variance also contributed to the year-over-year increase.

In the first nine months of 2022, fuel expense of \$3,817 million increased \$2,906 million or about four times from the same period of 2021 as a result of an 86% increase in jet fuel price and to the higher volume of flying compared to the same period in 2021.

Wages, Salaries and Benefits

Wages, salaries and benefits of \$816 million in the third quarter of 2022 increased \$224 million or 38% from the third quarter of 2021 and of \$2,272 million in the first nine months of 2022 increased \$655 million or 41% from the first nine months of 2021. The increases were mainly due to an increase in FTEs compared to the same period in 2021 as Air Canada significantly increased its staffing levels to support the increase in flying volume year-over-year, including in preparation for a continued ramp-up of activity levels for the remainder of the year.

Regional Airlines Expense

In the third quarter of 2022, regional airlines expense (excluding fuel and ownership costs) of \$400 million increased \$88 million or 28% from the third quarter of 2021 due to a higher volume of flying compared to the third quarter of 2021.

In the first nine months of 2022, regional airlines expense (excluding fuel and ownership costs) of \$1,083 million increased \$383 million or 55% from the same period in 2021 due to a higher volume of flying compared to the first nine months of 2021.

The following table provides a breakdown of regional airlines expense for the periods indicated.

(Canadian dollars in millions)	Third Quarter				First Nine Months			
	2022	2021	\$ Change	% Change	2022	2021	\$ Change	% Change
Capacity purchase fees ⁽¹⁾	\$ 194	\$ 167	\$ 27	16	\$ 549	\$ 394	\$ 155	39
Airport and navigation	67	54	13	24	170	95	75	79
Sales and distribution costs	33	15	18	120	73	24	49	204
Other operating expenses	106	76	30	39	291	187	104	56
Total regional airlines expense	\$ 400	\$ 312	\$ 88	28	\$ 1,083	\$ 700	\$ 383	55

(1) Capacity purchase fees exclude the component of fees related to aircraft ownership costs which are accounted for as lease liabilities in accordance with IFRS 16 – Leases.

Aircraft Maintenance

In the third quarter of 2022, aircraft maintenance expense of \$193 million increased \$40 million or 26% from the third quarter of 2021. The increase was largely due to higher maintenance activity due to higher volume of flying compared to the same period in 2021. Savings resulting from an amended agreement with a third-party maintenance provider, as further described below, partially offset the year-over-year increase. To a lesser extent, a year-over-year increase in maintenance provisions reflecting updated end-of-lease cost estimates, in anticipation of returning aircraft to lessors upon lease expiries over the next 12 months, also contributed to the increase.

In the first nine months of 2022, aircraft maintenance expense of \$414 million decreased \$16 million or 4% from the first nine months of 2021. In the first quarter of 2022, Air Canada and a third-party maintenance provider completed an amended agreement. In connection with this, a favourable adjustment of \$159 million was recorded in Aircraft maintenance expense arising from the adjustment to maintenance accruals and recognition of future credits that will be available under the amended agreement. Given the significantly reduced aircraft operations and fleet reductions during the COVID-19 pandemic, this agreement was amended by the parties to convert the nature of the services from a power-by-the-hour basis to a time and materials contract and reduced the number of items covered under the agreement. The expense reduction was partially offset by increased volume of maintenance activity resulting from the increased flying year-over-year and by an increase in maintenance provisions reflecting updated end-of-lease cost estimates in anticipation of returning aircraft to lessors upon lease expiries over the next 12 months.

Ground Package Costs

In the third quarter and in the first nine months of 2022, ground package costs of \$80 million and of \$311 million increased \$57 million and \$282 million from the same period in 2021, respectively. The increases were largely due to a higher volume of ground package revenues at Air Canada Vacations for the respective periods. Air Canada suspended its flights to Mexico and Caribbean destinations between January 31, 2021 and June 26, 2021.

Special Items

In the third quarter of 2022, Air Canada did not record any special items. The table below provides the breakdown of the special items recorded for the periods identified.

(Canadian dollars in millions)	Third Quarter		First Nine Months	
	2022	2021	2022	2021
Impairments (impairment reversal)	\$ -	\$ (12)	\$ 4	\$ 14
Government wage subsidy, net	-	(103)	-	(424)
Workforce reduction provisions	-	4	-	163
Benefit plan amendments	-	8	-	76
Other	-	-	-	14
Special Items	\$ -	\$ (103)	\$ 4	\$ (157)

Impairments

In the first nine months of 2021, an impairment charge of \$14 million was recorded as a result of reductions to the estimates around the expected disposal proceeds on owned aircraft, partially offset by lower-than-expected costs to meet contractual return conditions on lease returns. An impairment charge of \$4 million was recorded in the first nine months of 2022 related to the return of leased aircraft. Further changes to these estimates may result in additional adjustments to the impairment charge in future periods.

Government Wage Subsidy

No wage subsidy was recorded in the first nine months of 2022 as Air Canada no longer qualified under the available programs (gross subsidy of \$103 million in the third quarter of 2021; \$103 million net of costs; gross subsidy of \$429 million for the nine months ended September 30, 2021; \$424 million net of costs).

Workforce Reduction Provisions

As a result of the COVID-19 pandemic and to mitigate the number of employees who were on layoff status, during the second quarter of 2021, Air Canada offered early retirement incentive programs to its unionized workforce. These programs provided for pension improvements which were payable from the defined benefit pension plan for eligible employees, and as such did not impact Air Canada's liquidity position. Termination benefits and a curtailment loss of \$163 million were recorded for the nine months ended September 30, 2021 as a special item.

Benefit Plan Amendments

In April 2021, Air Canada received the decision of the arbitrator determining the cap on pensionable earnings recognized in the defined benefit pension plan for IAMAW-represented technical employees. The decision resulted in an increase to the maximum pensionable earnings, effective from 2021, with retroactivity to 2019 for employees that so elected. Air Canada recorded a one-time pension past service cost of \$76 million as a special item for the nine months ended September 30, 2021 as a result of this plan amendment. An additional \$6 million was recorded in the fourth quarter of 2021 as a special item. This amendment did not impact Air Canada's liquidity position as it is funded out of the surplus in the domestic registered pension plans.

OtherTermination of the Transat Arrangement Agreement

In April 2021, Air Canada announced that the arrangement agreement for the proposed acquisition by Air Canada of Transat A.T. Inc ("Transat") was terminated, including the payment of a \$12.5 million termination fee to Transat. The termination fee was recorded as a Special item during the first quarter of 2021.

Amendments to Capacity Purchase Agreements

In March 2021, Air Canada announced an agreement to amend the capacity purchase agreement ("Jazz CPA") with Jazz, under which Jazz currently operates regional flights under the Air Canada Express brand. Through the revised agreement, Air Canada transferred the operation of its Embraer E175 fleet to Jazz from Sky Regional and Jazz became the sole operator of flights under the Air Canada Express brand. The capacity purchase agreement with Sky Regional was terminated. Air Canada recorded a net expense of \$2 million, related to the CPA revisions and consolidation of regional flying.

Other operating expenses

In the third quarter and in the first nine months of 2022, other operating expenses of \$411 million and of \$1,083 million increased \$170 million and \$495 million from same period in 2021, respectively. The increases are primarily due to an increased level of flying year-over-year.

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

(Canadian dollars in millions)	Third Quarter				First Nine Months			
	2022	2021	\$ Change	% Change	2022	2021	\$ Change	% Change
Terminal handling	\$ 83	\$ 44	\$ 39	89	\$ 212	\$ 106	\$ 106	100
Crew cycle	58	29	29	100	148	57	91	160
Building rent and maintenance	53	36	17	47	139	99	40	40
Miscellaneous fees and services	57	39	18	46	145	107	38	36
Remaining other expenses	160	93	67	72	439	219	220	100
Total other expenses	\$ 411	\$ 241	\$ 170	71	\$ 1,083	\$ 588	\$ 495	84

Non-Operating Expense

In the third quarter of 2022, total non-operating expense was \$1,148 million compared to \$315 million in the third quarter of 2021. In the first nine months of 2022, total non-operating expense was \$1,511 million compared to \$818 million in the first nine months of 2021.

For both periods, the most notable changes were due to the foreign exchange variance as compared to the same periods in 2021.

Losses on foreign exchange of \$951 million in the third quarter of 2022 and of \$1,048 million in the first nine months of 2022 compared to losses of \$136 million in the third quarter of 2021 and of \$74 million in the first nine months of 2021. The September 30, 2022 closing exchange rate was US\$1=\$1.3829 compared to US\$1=\$1.2873 at June 30, 2022. The variances were mainly due to foreign exchange remeasurement on long-term debt and lease obligations of \$862 million in the third quarter of 2022 and of \$1,066 million in the first nine months of 2022.

Interest expense of \$239 million in the third quarter of 2022 and of \$664 million in the first nine months of 2022 compared to \$197 million in the third quarter of 2021 and of \$538 million in the first nine months of 2021. The increases were mainly due to higher levels of debt as a result of the financing transactions concluded during 2021, and to a lesser extent, unfavourable changes in interest and foreign exchange rates.


Air Canada recorded a loss of \$25 million on financial instruments recorded at fair value in the third quarter of 2022 compared to a gain of \$114 million in the third quarter of 2021, and a gain of \$89 million in the first nine months of 2022 compared to a loss of \$114 million in the first nine months of 2021. The fluctuation in the fair value of Air Canada's convertible notes resulted in a loss of \$22 million in the third quarter of 2022 and in a gain of \$174 million in the first nine months of 2022. The fluctuation in the fair value of Air Canada's short-term investments resulted in a loss of \$3 million in the third quarter of 2022 and a loss of \$84 million in the first nine months of 2022.

In the third quarter of 2022, Air Canada recorded a \$17 million gain on debt settlement related to the repurchase of \$273 million (US\$207 million) aggregate principal amount of its outstanding 4.000% Convertible Senior Notes due 2025 for an aggregate cash repurchase price of approximately \$329 million (US\$249 million), including accrued interest.

6. FLEET

The tables below provide the number of aircraft in Air Canada's and Air Canada Rouge's operating fleet as at December 31, 2021 and as at September 30, 2022, as well as the planned fleet for the future periods indicated.

The tables below include certain aircraft that were grounded in response to the COVID-19 pandemic. As at September 30, 2022, four aircraft remained grounded pending return to service maintenance. In the second quarter of 2022, Air Canada took delivery of two new Boeing 767 freighter aircraft which are expected to enter service in 2023; these aircraft are included in the table below.

 AIR CANADA	Actual			Planned			
	Dec. 31, 2021	First Nine Months of 2022 Fleet Changes	Sep. 30, 2022	Remainder 2022 Fleet Changes	Dec. 31, 2022	2023 Fleet Changes	Dec. 31, 2023
Wide-body aircraft							
Boeing 777-300ER	11	7	18	-	18	-	18
Boeing 777-300ER (cargo)	7	(7)	-	-	-	-	-
Boeing 777-200LR	6	-	6	-	6	-	6
Boeing 787-8	8	-	8	-	8	-	8
Boeing 787-9	29	-	29	-	29	2	31
Boeing 767-300 freighters	1	3	4	2	6	1	7
Airbus A330-300	12	4	16	1	17	1	18
Airbus A330-300 (cargo)	4	(4)	-	-	-	-	-
Total wide-body aircraft	78	3	81	3	84	4	88
Narrow-body aircraft							
Boeing 737 MAX 8	31	9	40	-	40	-	40
Airbus A321	15	-	15	-	15	-	15
Airbus A320	18	-	18	(2)	16	-	16
Airbus A319	6	-	6	(3)	3	-	3
Airbus A220-300	27	4	31	2	33	-	33
Total narrow-body aircraft	97	13	110	(3)	107	-	107
Total Mainline	175	16	191	-	191	4	195




	Actual			Planned			
	Dec. 31, 2021	First Nine Months of 2022 Fleet Changes	Sep. 30, 2022	Remainder 2022 Fleet Changes	Dec. 31, 2022	2023 Fleet Changes	Dec. 31, 2023
Narrow-body aircraft							
Airbus A321	14	-	14	3	17	-	17
Airbus A320	5	-	5	-	5	-	5
Airbus A319	20	-	20	-	20	-	20
Total Air Canada Rouge	39	-	39	3	42	-	42

Total Mainline & Rouge	214	16	230	3	233	4	237
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Air Canada Express

The table below provides the number of aircraft operated as at December 31, 2021 and as at September 30, 2022, on behalf of Air Canada, by its regional carrier operating flights under the Air Canada Express banner pursuant to a capacity purchase agreement with Air Canada. The table also provides the planned fleet for the future periods indicated.

	Actual			Planned			
	Dec. 31, 2021	First Nine Months of 2022 Fleet Changes	Sep. 30, 2022	Remainder 2022 Fleet Changes	Dec. 31, 2022	2023 Fleet Changes	Dec. 31, 2023
							
Embraer 175	25	-	25	-	25	-	25
Mitsubishi CRJ-200	15	-	15	-	15	-	15
Mitsubishi CRJ-900	35	-	35	-	35	-	35
De Havilland Dash 8-300	9	(9)	-	-	-	-	-
De Havilland Dash 8-400	39	-	39	-	39	(3)	36
Total Air Canada Express	123	(9)	114	-	114	(3)	111

7. FINANCIAL AND CAPITAL MANAGEMENT

7.1 LIQUIDITY

Impact of the COVID-19 Pandemic

One of Air Canada's key objectives is to return to sustainable profitability and to sustain and improve cash flows from operations to manage its liquidity needs. Air Canada has recently seen a progressive improvement in cash flows from operating activities. Considering the uncertainty brought about by the COVID-19 pandemic, the recent challenges faced by the global airline industry to meet the surge in traffic, the volatility of aircraft fuel prices, and geopolitical, economic, and other factors, the timing and extent of the return to sustained pre-pandemic traffic levels remains difficult to predict.

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 7.6 "Capital Expenditures and Related Financing Arrangements", 7.7 "Pension Funding Obligations", and 7.8 "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 September 30, 2022 total liquidity was \$10,236 million comprised of cash and cash equivalents, short-term and long-term investments of \$9,206 million, and \$1,030 million available under undrawn credit facilities.

Air Canada estimates that it requires a minimum total liquidity balance of \$5,000 million to support ongoing business operations, updated from the \$2,400 million amount as reported at December 31, 2021. This minimum cash estimate considers Air Canada's various financial covenants, provides adequate coverage for advance ticket sales, and supports Air Canada's liquidity needs, as described above. The increase in the minimum liquidity balance from the amount reported at December 31, 2021 reflects the increasing scale of operations as Air Canada continues to rebuild the airline and also includes a larger buffer to manage cost risk and unplanned disruptions. Minimum total liquidity includes funds available under credit facilities.

7.2 FINANCIAL POSITION

The table below provides a condensed consolidated statement of financial position of Air Canada as at September 30, 2022, and as at December 31, 2021.

(Canadian dollars in millions)	September 30, 2022	December 31, 2021	\$ Change
Assets			
Cash, cash equivalents and short-term investments	\$ 8,490	\$ 8,969	\$ (479)
Other current assets	1,705	1,084	621
Current assets	\$ 10,195	\$ 10,053	\$ 142
Investments, deposits, and other assets	964	858	106
Property and equipment	11,885	11,740	145
Pension assets	2,334	3,571	(1,237)
Deferred income tax	49	39	10
Intangible assets	1,054	1,080	(26)
Goodwill	3,273	3,273	-
Total assets	\$ 29,754	\$ 30,614	\$ (860)
Liabilities			
Current liabilities	\$ 9,005	\$ 6,924	\$ 2,081
Long-term debt and lease liabilities	15,799	15,511	288
Aeroplan and other deferred revenues	3,195	3,656	(461)
Pension and other benefit liabilities	1,850	2,588	(738)
Maintenance provisions	1,293	1,032	261
Other long-term liabilities	470	821	(351)
Deferred income tax	73	73	-
Total liabilities	\$ 31,685	\$ 30,605	\$ 1,080
Total shareholders' equity (deficiency)	\$ (1,931)	\$ 9	\$ (1,940)
Total liabilities and shareholders' equity (deficiency)	\$ 29,754	\$ 30,614	\$ (860)

Movements in current assets and current liabilities are described in section 7.4 "Working Capital" of this MD&A. Long-term debt and lease liabilities are discussed in sections 7.3 "Net Debt" and 7.5 "Cash Flow Movements" of this MD&A.

At September 30, 2022, net long-term benefit assets of \$484 million (comprising pension assets of \$2,334 million net of pension and other benefit liabilities of \$1,850 million) decreased \$499 million from December 31, 2021. This decrease was mainly due to a net actuarial loss on remeasurements of employee liabilities of \$251 million (\$75 million, net of tax) recorded on Air Canada's consolidated statement of comprehensive income, as well as pension and other employee benefits expense recorded during the year. The actuarial loss reflects the limit on the amount of pension assets that can be recognized under the accounting rules. While the actuarial gain on the 193-basis point increase in discount rate used to value the liabilities offset a lower return on plan assets, the net asset that could be recognized was capped to the amount of surplus available to reduce future funding requirements.

The long-term portion of the Aeroplan and other deferred revenue liability decreased \$461 million from December 31, 2021. This decrease included a reclassification of \$293 million from long-term to current liabilities for Aeroplan Point redemptions

expected to occur over the next 12 months, as well as Aeroplan Point redemptions exceeding the sale of points to program partners. The decrease to Other long-term liabilities included a \$301 million decrease in the fair value liability of the embedded derivative on Air Canada's convertible notes of which \$127 million was recognized on the repurchase of the convertible notes.

7.3 NET DEBT

The table below reflects Air Canada's net debt balances as at September 30, 2022, and as at December 31, 2021.

(Canadian dollars in millions)	September 30, 2022	December 31, 2021	\$ Change
Total long-term debt and lease liabilities	\$ 15,799	\$ 15,511	\$ 288
Current portion of long-term debt and lease liabilities	1,236	1,012	224
Total long-term debt and lease liabilities (including current portion)	17,035	16,523	512
Less cash, cash equivalents and short and long-term investments	(9,206)	(9,570)	364
Net debt ⁽¹⁾	\$ 7,829	\$ 6,953	\$ 876

(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. For additional information on net debt, refer to section 16 "Non-GAAP Financial Measures" of this MD&A.*

As at September 30, 2022, net debt of \$7,829 million increased \$876 million from December 31, 2021. The unfavorable impact of a weaker Canadian dollar at September 30, 2022 compared to December 31, 2021, increased foreign currency denominated debt (mainly U.S. dollars) by \$1,068 million. The change in long-term debt and lease liabilities also included \$1,074 million of repayments, comprised of regularly scheduled repayments and \$326 million for the repurchase of convertible notes.

7.4 WORKING CAPITAL

The table below provides information on Air Canada's working capital balances as at September 30, 2022 and as at December 31, 2021.

(Canadian dollars in millions)	September 30, 2022	December 31, 2021	\$ Change
Cash, cash equivalents and short-term investments	\$ 8,490	\$ 8,969	\$ (479)
Accounts receivable	1,013	691	322
Other current assets	692	393	299
Total current assets	\$ 10,195	\$ 10,053	\$ 142
Accounts payable and accrued liabilities	2,495	2,603	(108)
Advance ticket sales	3,998	2,326	1,672
Aeroplan and other deferred revenues	1,276	983	293
Current portion of long-term debt and lease liabilities	1,236	1,012	224
Total current liabilities	\$ 9,005	\$ 6,924	\$ 2,081
Net working capital	\$ 1,190	\$ 3,129	\$ (1,939)

Net working capital of \$1,190 million as at September 30, 2022 decreased \$1,939 million from December 31, 2021. This decrease was mainly due to a combination of net cash outflows relating to capital expenditures and debt repayments in the first nine months of 2022, partially offset by positive operating cash results. The increases in accounts receivable, other current assets and advance ticket sales are mainly driven by the passenger sales demand which is supported with the increased capacity.

7.5 CASH FLOW MOVEMENTS

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

(Canadian dollars in millions)	Third Quarter			First Nine Months		
	2022	2021	\$ Change	2022	2021	\$ Change
Net cash flows from (used in) operating activities	\$ 290	\$ 305	\$ (15)	\$ 1,721	\$ (2,010)	\$ 3,731
Proceeds from borrowings	41	6,760	(6,719)	202	8,027	(7,825)
Reduction of long-term debt and lease liabilities	(573)	(2,953)	2,380	(1,074)	(4,234)	3,160
Issue of shares	2	-	2	4	554	(550)
Financing fees	(4)	(196)	192	(5)	(203)	198
Net cash flows from (used in) financing activities	\$ (534)	\$ 3,611	\$ (4,145)	\$ (873)	\$ 4,144	\$ (5,017)
Investments, short-term and long-term	276	(1,299)	1,575	(1,394)	51	(1,445)
Additions to property, equipment, and intangible assets	(333)	(149)	(184)	(1,245)	(695)	(550)
Proceeds from sale of assets	4	5	(1)	9	16	(7)
Proceeds from sale and leaseback of assets	-	-	-	-	11	(11)
Other	(3)	20	(23)	(5)	15	(20)
Net cash flows used in investing activities	\$ (56)	\$ (1,423)	\$ 1,367	\$ (2,635)	\$ (602)	\$ (2,033)
Effect of exchange rate changes on cash and cash equivalents	\$ -	\$ 53	\$ (53)	\$ 18	\$ 16	\$ 2
Increase (decrease) in cash and cash equivalents	\$ (300)	\$ 2,546	\$ (2,846)	\$ (1,769)	\$ 1,548	\$ (3,317)

Net Cash Flows from (used in) Operating Activities

Net cash flows from operating activities were \$290 million in the third quarter of 2022. While net cash from earnings increased \$1 billion over the same period in 2021, in-line with the increase in EBITDA (excluding special items), the change in working capital items decreased by a similar amount as the third quarter of 2021 reflected a significant recovery in advance ticket sale levels in that period, whereas the change in advance ticket sales in third quarter of 2022 had largely normalized.

In the first nine months of 2022, net cash flows from operating activities of \$1,721 million improved by \$3,731 million from the same period in 2021. The improvement was due to strong advance ticket sales and positive cash from operating results when compared to the same period in 2021. Additionally, the first nine months of 2021 included cash outflows from operating activities of \$1,208 million related to the refund of non-refundable fares.

Net Cash Flows from (used in) Financing Activities

In September 2022, Air Canada repurchased \$273 million (US\$207 million) aggregate principal amount of its outstanding 4.000% Convertible Senior Notes due 2025 for an aggregate cash repurchase price of approximately \$329 million (US\$249 million), including accrued interest. The third quarter of 2021 included net proceeds of \$3.7 billion related to the refinancing transactions completed in August 2021 and further described in section 4 "2021 Highlights" of Air Canada's 2021 MD&A.

Net Cash Flows from (used in) Investing Activities

Net movements between cash and short and long-term investments amounted to \$276 million and (\$1,394) million during the third quarter of 2022 and the first nine months of 2022, respectively. Additions to property, equipment and intangible assets for the nine months of 2022 of \$1,245 million increased \$550 million from the same period in 2021. These additions relate mainly to aircraft acquisitions and related pre-delivery payments, capitalized maintenance and technology projects.

Refer to sections 7.2 "Financial Position", 7.3 "Net Debt", and 7.4 "Working Capital" of this MD&A for additional information.

Free Cash Flow

The table below provides the calculation of free cash flow⁽¹⁾ for Air Canada for the periods indicated.

(Canadian dollars in millions)	Third Quarter			First Nine Months		
	2022	2021	\$ Change	2022	2021	\$ Change
Net cash flows from (used in) operating activities	\$ 290	\$ 305	\$ (15)	\$ 1,721	\$ (2,010)	\$ 3,731
Additions to property, equipment, and intangible assets, net of proceeds from sale and leaseback transactions	(333)	(149)	(184)	(1,245)	(684)	(561)
Free cash flow ⁽¹⁾	\$ (43)	\$ 156	\$ (199)	\$ 476	\$ (2,694)	\$ 3,170

(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, 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 16 "Non-GAAP Financial Measures" of this MD&A for additional information.

Negative free cash flow of \$43 million in the third quarter of 2022 decreased by \$199 million from the same period in 2021 mainly due to a higher level of capital expenditures year-over-year. Free cash flow of \$476 million in the first nine months of 2022 improved \$3,170 million from the same period in 2021, reflecting higher net cash flows from operations as a result of an improved operating environment and strong advance ticket sales.

7.6 CAPITAL EXPENDITURES AND RELATED FINANCING ARRANGEMENTS

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 2024 with the final aircraft to arrive in 2027. Of the 30 total aircraft, 20 aircraft will be leased and 10 are being acquired under a purchase agreement with Airbus S.A.S. that includes purchase rights to acquire up to an additional 15 aircraft between 2027 and 2030.

Airbus A220-300 Aircraft

Air Canada's agreement with Airbus Canada for the purchase of Airbus A220-300 aircraft provides for:

- Firm orders for 60 Airbus A220-300 aircraft, 15 of which result from Air Canada's exercise of options for the same number of Airbus A220 aircraft as described below.
- Purchase options for 15 additional Airbus A220-300 aircraft.

In January 2022, Air Canada elected to proceed with the purchase of an additional 10 Airbus A220 aircraft, in addition to the two Airbus A220 aircraft that were added in 2021. These 12 aircraft are those that Air Canada had stated, in November 2020, it would no longer be purchasing. Planned deliveries for the 12 aircraft are: six in 2024, and six in 2025.

In the third quarter of 2022, Air Canada elected to exercise options for an additional 15 Airbus A220 aircraft which are expected to be delivered in 2026.

In March 2021, Air Canada had concluded a committed secured facility totalling US\$475 million to finance the purchase of the next 15 Airbus A220 aircraft scheduled for delivery in 2021 and 2022. Financing has been used for 13 Airbus A220 aircraft. Financing remains available for an additional two aircraft under this facility.

As at September 30, 2022, 31 Airbus A220-300 aircraft had been delivered.

Boeing 737 MAX

Air Canada's agreement with Boeing for the purchase of Boeing 737 MAX aircraft provides for:

- Purchase options for 10 Boeing 737 MAX aircraft

At September 30, 2022, all 40 Boeing 737 MAX 8 aircraft on firm order had been delivered.

Boeing 787-9 Aircraft

Air Canada exercised options for the purchase of three Boeing 787-9 aircraft which are scheduled to be delivered in 2023 and in 2024. Air Canada has no additional purchase options for Boeing 787 aircraft.

Boeing 767 Freighter Aircraft

Air Canada finalized an agreement for the purchase of two new Boeing 767 freighter aircraft which were delivered in the second quarter of 2022 and are expected to enter service in 2023. Air Canada expects to have a fleet of seven Boeing 767 freighters by the end of 2023 and expects to add a further three Boeing 767 freighters in 2024 and 2025.

Boeing 777 Freighter Aircraft

Air Canada finalized an agreement for the purchase of two new Boeing 777 freighter aircraft with deliveries expected in 2024.

Heart Aerospace ES-30 Electric Aircraft

In the third quarter of 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, however the agreement provides for a price cap. The regional aircraft are expected to enter service in 2028. In addition to the purchase agreement, Air Canada has entered into an agreement providing for a \$7 million (US\$5 million) investment by Air Canada in Heart Aerospace.

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 September 30, 2022 amounted to \$7,618 million.

(Canadian dollars in millions)	Remainder of 2022	2023	2024	2025	2026	Thereafter	Total
Committed expenditures	\$ 378	\$ 1,115	\$ 1,182	\$ 882	\$ 1,460	\$ 2,601	\$ 7,618
Projected planned but uncommitted expenditures	49	335	454	499	384	Not available	Not available
Projected planned but uncommitted capitalized maintenance ⁽¹⁾	107	387	482	471	494	Not available	Not available
Total projected expenditures ⁽²⁾	\$ 534	\$ 1,837	\$ 2,118	\$ 1,852	\$ 2,338	\$ 2,601	Not available

(1) Future capitalized maintenance amounts for 2025 and beyond are not yet determinable, however estimates of \$471 million and \$494 million have been made for 2025 and 2026, respectively.

(2) U.S. dollar amounts are converted using the September 30, 2022 closing exchange rate of US\$1=C\$1.3829. The estimated aggregate cost of aircraft is based on delivery prices that include estimated escalation and, where applicable, deferred price delivery payment interest calculated based on the 90-day U.S. LIBOR rate at September 30, 2022.

7.7 PENSION FUNDING OBLIGATIONS

As at January 1, 2022, the aggregate solvency surplus in Air Canada's domestic registered pension plans was \$4.8 billion.

Air Canada's pension funding obligations are discussed in section 9.7 "Pension Funding Obligations" of Air Canada's 2021 MD&A. There have been no material changes to Air Canada's pension funding obligations from what was disclosed at that time.

7.8 CONTRACTUAL OBLIGATIONS

The table below provides Air Canada's projected contractual obligations as at September 30, 2022, 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)	Remainder of 2022 ⁽²⁾	2023	2024	2025	2026	Thereafter	Total
Principal							
Long-term debt ⁽¹⁾	\$ 163	\$ 725	\$ 532	\$ 1,666	\$ 2,596	\$ 8,743	\$ 14,425
Lease liabilities	145	548	510	479	\$ 336	1,138	3,156
Total principal obligations	\$ 308	\$ 1,273	\$ 1,042	\$ 2,145	\$ 2,932	\$ 9,881	\$ 17,581
Interest							
Long-term debt	\$ 127	\$ 666	\$ 636	\$ 602	\$ 520	\$ 883	\$ 3,434
Lease liabilities	42	147	119	92	71	325	796
Total interest obligations	\$ 169	\$ 813	\$ 755	\$ 694	\$ 591	\$ 1,208	\$ 4,230
Total long-term debt and lease liabilities	\$ 477	\$ 2,086	\$ 1,797	\$ 2,839	\$ 3,523	\$ 11,089	\$ 21,811
Committed capital expenditures	\$ 378	\$ 1,115	\$ 1,182	\$ 882	\$ 1,460	\$ 2,601	\$ 7,618
Total contractual obligations ⁽²⁾	\$ 855	\$ 3,201	\$ 2,979	\$ 3,721	\$ 4,983	\$ 13,690	\$ 29,429

(1) Assumes the principal balance of the convertible notes, \$747 million (US\$540 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.

7.9 SHARE INFORMATION

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

	September 30, 2022	December 31, 2021
Issued and outstanding shares		
Class A variable voting shares	63,799,071	82,897,507
Class B voting shares	294,346,070	274,944,350
Total issued and outstanding shares	358,145,141	357,841,857
Class A variable voting and Class B voting shares potentially issuable		
Convertible notes	35,185,616	48,687,441
Warrants	-	7,288,282
Stock options	5,463,268	4,330,993
Total shares potentially issuable	40,648,884	60,306,716
Total outstanding and potentially issuable shares	398,794,025	418,148,573

Warrants

As described in section 9.9 "Share Information" of Air Canada's 2021 MD&A, Air Canada exercised its call right to purchase and cancel the 7,288,282 vested warrants at fair market value of \$82 million, with settlement completed in January 2022.

Convertible Notes

In September 2022, the Corporation repurchased and cancelled \$273 million (US\$207 million) aggregate principal amount of its convertible notes. The conversion rate of the convertible notes is 65.1337 shares per US\$1,000 principal amount of convertible notes, thereby reducing the potential issuable shares.

8. QUARTERLY FINANCIAL DATA

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

(Canadian dollars in millions, except per share figures)	2020	2021				2022		
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Operating revenues	\$ 827	\$ 729	\$ 837	\$ 2,103	\$ 2,731	\$ 2,573	\$ 3,981	\$ 5,322
Operating expenses	1,830	1,778	1,970	2,467	3,234	3,123	4,234	4,678
Operating income (loss)	(1,003)	(1,049)	(1,133)	(364)	(503)	(550)	(253)	644
Non-operating income (expense)	(272)	(338)	(165)	(315)	(114)	(264)	(99)	(1,148)
Loss before income taxes	(1,275)	(1,387)	(1,298)	(679)	(617)	(814)	(352)	(504)
Income tax recovery (expense)	114	83	133	39	124	(160)	(34)	(4)
Net loss	\$ (1,161)	\$ (1,304)	\$ (1,165)	\$ (640)	\$ (493)	\$ (974)	\$ (386)	\$ (508)
Diluted loss per share	\$ (3.91)	\$ (3.90)	\$ (3.31)	\$ (1.79)	\$ (1.38)	\$ (2.72)	\$ (1.60)	\$ (1.42)
Adjusted pre-tax loss⁽¹⁾	\$ (1,326)	\$ (1,335)	\$ (1,210)	\$ (649)	\$ (574)	\$ (740)	\$ (447)	\$ 446

(1) Adjusted pre-tax loss is a non-GAAP financial measure. For additional information, refer to section 16 "Non-GAAP Financial Measures" of this MD&A.

9. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Air Canada's financial instruments and risk management practices are summarized in section 12 "Financial Instruments and Risk Management" of Air Canada's 2021 MD&A. There have been no material changes to Air Canada's financial instruments and risk management practices from what was disclosed at that time. Additional information on Air Canada's risk management practices and financial instruments is provided in Note 9 of Air Canada's interim unaudited condensed consolidated financial statements for the third quarter of 2022.

10. ACCOUNTING POLICIES

Air Canada's accounting policies are consistent with those disclosed in Note 2 of Air Canada's 2021 annual consolidated financial statements except for the presentation of Restricted cash described below.

IAS 7 Statement of Cash Flows

In 2022, the IFRS Interpretations Committee finalized its decision that restrictions on the use of demand deposits arising from a contract with a third party do not preclude those deposits from being cash and cash equivalents when they are available to the company on demand. Therefore, they should be included in cash and cash equivalents in the statements of cash flows and financial position, with disclosure provided on significant cash and cash equivalents balances with restrictions on use.

Previously, Air Canada recorded Restricted cash under current assets representing funds held in trust by Air Canada Vacations in accordance with regulatory requirements governing advance sales for tour operators. While these funds are in trust pursuant to the applicable regulations, Air Canada may access these funds as services are rendered or as disbursements are made on behalf of the customer. As a result of this guidance on application of IAS 7 Statement of Cash Flows, Air Canada has reclassified these amounts to Cash and cash equivalents with the 2021 comparative figures also reclassified. Cash and cash equivalents include \$231 million related to these funds at September 30, 2022 (\$167 million at December 31, 2021).

11. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Air Canada's critical accounting estimates and judgments are summarized in section 14 "Critical Accounting Estimates and Judgments" of Air Canada's 2021 MD&A. There have been no material changes to critical accounting estimates and judgments from what was disclosed at that time.

12. OFF-BALANCE SHEET ARRANGEMENTS

Air Canada's off-balance sheet arrangements are summarized in section 15 "Off-Balance Sheet Arrangements" of Air Canada's 2021 MD&A. There have been no material changes to Air Canada's off-balance sheet arrangements from what was disclosed at that time.

13. RELATED PARTY TRANSACTIONS

At September 30, 2022, 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.

14. RISK FACTORS

For a description of risk factors associated with Air Canada and its business, refer to section 18 "Risk Factors" of Air Canada's 2021 MD&A. There have been no material changes to Air Canada's risk factors from what was disclosed at that time, except for the following.

During the period from March 2020 until early 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, but the wide-ranging impact of the COVID-19 pandemic and certain other factors have impeded, particularly during the summer of 2022, Air Canada's and the global airline industry's restart efforts and also the ability of some of its participants, on which Air Canada's operations are dependent, to support the surge in traffic. Over the period from June to August, this led to a meaningful increase in flight delays and cancellations, and other operational disruptions and challenges. Flight delays and cancellations started to decrease in August and there was a progressive increase in operational stability experienced in the second half of the third quarter of 2022, however there can be no assurance that further significant disruptions will not reoccur. The impact of the COVID-19 pandemic continues to evolve, amplifying or adding new risks, including economic risks, any of which could materially and adversely affect Air Canada's business, results from operations, financial condition.

15. CONTROLS AND PROCEDURES

Air Canada's controls and procedures are summarized in section 19 "Controls and Procedures" of Air Canada's 2021 MD&A. There have been no material changes to Air Canada's controls and procedures from what was disclosed at that time.

16. 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.

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. Air Canada excludes special items from EBITDA as these items may distort the analysis of certain business trends and render comparative analysis across periods or to other airlines less meaningful.

EBITDA Margin

EBITDA margin (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.

Operating Margin

Operating margin (operating income (loss) as a percentage of operating revenues) is commonly used in the airline industry and is used by Air Canada as a means to view profitability after operating expenses before interest and taxes.

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

(Canadian dollars in millions, except where indicated)	Third Quarter			First Nine Months		
	2022	2021	Change	2022	2021	Change
Operating income (loss) – GAAP	\$ 644	\$ (364)	\$ 1,008	\$ (159)	\$ (2,546)	\$ 2,387
Add back:						
Depreciation and amortization	413	400	13	1,223	1,217	6
EBITDA (including special items)	\$ 1,057	\$ 36	\$ 1,021	\$ 1,064	\$ (1,329)	\$ 2,393
Remove:						
Special items	-	(103)	103	4	(157)	161
EBITDA (excluding special items)	\$ 1,057	\$ (67)	\$ 1,124	\$ 1,068	\$ (1,486)	\$ 2,554
Operating revenues	\$ 5,322	\$ 2,103	\$ 3,219	\$ 11,876	\$ 3,669	\$ 8,207
Operating margin (%)	12.1	(17.3)	29.4 pp	(1.3)	(69.4)	68.1 pp
EBITDA margin (%)	19.9	(3.2)	23.1 pp	9.0	(40.5)	49.5 pp

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, freighter costs, and special items as these items may distort the analysis of certain business trends and render comparative analysis across periods or to other airlines less meaningful.

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 introduced one Boeing 767 dedicated freighter to its operating fleet in December 2021 and added a second Boeing 767 freighter in April 2022. In the second quarter of 2022, Air Canada took delivery of two new Boeing 767 freighter aircraft, which are expected to enter service in 2023. Air Canada expects to have a fleet of seven Boeing 767 dedicated freighters by the end of 2023 and expects to add a further three Boeing 767 freighters in 2024 and 2025 as well as two new Boeing 777 freighter aircraft with deliveries expected in 2024. Prior to 2021, Air Canada did not incur any costs related to the operation of dedicated freighter aircraft. 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.

Excluding aircraft fuel expense, the cost of ground packages at Air Canada Vacations, dedicated freighter expenses and special items from operating expenses generally allows for a more meaningful analysis of Air Canada's operating expense performance and a more meaningful comparison to that of other airlines.

Adjusted CASM is reconciled to GAAP operating expense as follows:

(Canadian dollars in millions, except where indicated)	Third Quarter			First Nine Months		
	2022	2021	Change	2022	2021	Change
Operating expense – GAAP	\$ 4,678	\$ 2,467	\$ 2,211	\$ 12,035	\$ 6,215	\$ 5,820
Adjusted for:						
Aircraft fuel	(1,617)	(472)	(1,145)	(3,817)	(911)	(2,906)
Ground package costs	(80)	(23)	(57)	(311)	(29)	(282)
Special items	-	103	(103)	(4)	157	(161)
Freighter costs (excluding fuel)	(26)	-	(26)	(59)	-	(59)
Operating expense, adjusted for the above-noted items	\$ 2,955	\$ 2,075	\$ 880	7,844	5,432	2,412
ASMs (millions)	25,562	11,116	130.0%	60,190	19,327	211.4%
Adjusted CASM (cents)	¢ 11.56	¢ 18.65	¢ (7.09)	¢ 13.03	¢ 28.10	¢ (15.07)

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 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, and special items 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:

(Canadian dollars in millions)	Third Quarter			First Nine Months		
	2022	2021	\$ Change	2022	2021	\$ Change
Loss before income taxes – GAAP	\$ (504)	\$ (679)	\$ 175	\$ (1,670)	\$ (3,364)	\$ 1,694
Adjusted for:						
Special items	-	(103)	103	4	(157)	161
Foreign exchange loss	951	136	815	1,048	74	974
Net interest relating to employee benefits	(9)	1	(10)	(17)	10	(27)
(Gain) loss on financial instruments recorded at fair value	25	(114)	139	(89)	114	(203)
(Gain) loss on debt settlements and modifications	(17)	110	(127)	(17)	129	(146)
Adjusted pre-tax income (loss)	\$ 446	\$ (649)	\$ 1,095	\$ (741)	\$ (3,194)	\$ 2,453

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 7.5 "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 7.3 "Net Debt" of this MD&A for a reconciliation of this capital management measure to the nearest measure under GAAP.

17. GLOSSARY

Adjusted CASM – Refers to operating expense per ASM adjusted to remove the effects of aircraft fuel expense, ground packages costs at Air Canada Vacations, special items, and freighter costs. Adjusted CASM is a non-GAAP financial measure. Refer to section 16 “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 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 debt settlements and modifications, gains or losses on disposal of assets, and special items. Adjusted pre-tax income (loss) is a non-GAAP financial measure. Refer to section 16 “Non-GAAP Financial Measures” of this MD&A for additional information.

Aeroplan – Refers to Aeroplan Inc.

Atlantic – In reference to passenger and cargo revenues, means 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 - In reference to passenger and cargo revenues, means revenues from flights within Canada.

EBITDA – Refers to earnings before interest, taxes, depreciation and amortization. EBITDA is a non-GAAP financial measure. Refer to section 16 “Non-GAAP Financial Measures” of this MD&A for additional information. Air Canada excludes special items from EBITDA.

EBITDA margin – Refers to EBITDA as a percentage of operating revenue. Refer to section 16 “Non-GAAP Financial Measures” of this MD&A for additional information.

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 7.5 “Cash Flow Movements” and 16 “Non-GAAP Financial Measures” of this MD&A for additional information.

Jazz – Refers to Jazz Aviation LP.

Jazz CPA – Refers to the capacity purchase agreement between Air Canada and Jazz.

Net debt – Refers to total long-term debt liabilities (including current portion) less cash, cash equivalents, and short- and long-term investment. Refer to section 7.3 “Net Debt” of this MD&A for a reconciliation of this non-GAAP financial measure to the nearest measure under GAAP.

Other - In reference to passenger and cargo revenues, means revenues from flights with origins and destinations principally in Central and South America, the Caribbean and Mexico.

Pacific - In reference to passenger and cargo revenues, means 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 Available Seat Miles.

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

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 (IATA) 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.

Special items – Refers to those items that, in management's view, are to be separately disclosed by virtue of their significance to the financial statements, to enable a fuller understanding of the Air Canada's financial performance.

Yield – Refers to average passenger revenue per RPM.