

**AVIATION CAPITAL GROUP LLC  
AND SUBSIDIARIES**

Unaudited Condensed Consolidated Financial Statements  
as of March 31, 2018 and December 31, 2017 and for the  
three months ended March 31, 2018 and 2017

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

<i>(In Thousands)</i>	March 31, 2018	December 31, 2017
<b>ASSETS</b>		
Cash and cash equivalents	\$161,444	\$166,875
Restricted cash	213,991	206,168
Flight equipment held for lease, net	7,694,631	7,424,227
Assets held for sale	361,093	410,073
Prepayments on flight equipment	1,128,910	1,174,046
Investment in finance leases, net	327,265	332,648
Derivative financial instruments at fair value, net	9,581	—
Equity method investments	6,569	25,622
Other assets, net	107,485	107,217
<b>TOTAL ASSETS</b>	<b>\$10,010,969</b>	<b>\$9,846,876</b>
<b>LIABILITIES AND EQUITY</b>		
Liabilities:		
Accounts payable, accrued expenses and other liabilities	\$152,505	\$139,143
Debt financings, net	5,953,650	5,900,839
Maintenance reserves	663,976	638,122
Security deposits	130,740	129,231
Deferred income	57,065	55,569
Lease incentives	23,061	21,126
Deferred income taxes, net	2,608	1,953
Derivative financial instruments at fair value, net	—	4,684
<b>TOTAL LIABILITIES</b>	<b>6,983,605</b>	<b>6,890,667</b>
Commitments and contingencies (Note 11)		
Equity:		
Members' equity	3,030,949	2,961,215
Accumulated other comprehensive loss	(3,585)	(5,006)
<b>TOTAL MEMBERS' EQUITY</b>	<b>3,027,364</b>	<b>2,956,209</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$10,010,969</b>	<b>\$9,846,876</b>

See Notes to Condensed Consolidated Financial Statements

*Aviation Capital Group LLC and Subsidiaries*

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

<i>(In Thousands)</i>	Three Months Ended March 31,	
	2018	2017
<b>REVENUES</b>		
Operating lease revenue	\$220,368	\$212,413
Amortization of lease incentives and premiums, net	(5,395)	(5,049)
Finance lease revenue	5,609	4,798
Gain on sale of flight equipment	2,472	7,169
Maintenance revenue	—	9,842
Other income	10,155	3,532
<b>TOTAL REVENUES</b>	<b>233,209</b>	<b>232,705</b>
<b>EXPENSES</b>		
Depreciation	82,448	80,431
Interest, net	56,467	56,113
Operating lease expense	5,790	5,824
Maintenance and transition expense	2,078	4,171
Asset impairment	492	125,149
Selling, general and administrative	17,913	14,887
<b>TOTAL EXPENSES</b>	<b>165,188</b>	<b>286,575</b>
Income (loss) before provision for (benefit from) income taxes and earnings from equity method investments	68,021	(53,870)
Provision for (benefit from) income taxes	538	(882,522)
Earnings from equity method investments	2,251	1,204
<b>NET INCOME</b>	<b>\$69,734</b>	<b>\$829,856</b>

See Notes to Condensed Consolidated Financial Statements

*Aviation Capital Group LLC and Subsidiaries*

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

<i>(In Thousands)</i>	Three Months Ended March 31,	
	2018	2017
<b>NET INCOME</b>	\$69,734	\$829,856
Other comprehensive income:		
Unrealized gain on interest rate swap contracts, net of taxes of \$32 and \$552	1,262	821
Reclassification into earnings from accumulated other comprehensive loss for de-designated hedges (included in interest, net)	159	302
<b>COMPREHENSIVE INCOME</b>	<b>\$71,155</b>	<b>\$830,979</b>

See Notes to Condensed Consolidated Financial Statements

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED STATEMENTS OF EQUITY

(Unaudited)

<i>(In Thousands)</i>	Members' Equity	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Equity
<b>BALANCES, JANUARY 1, 2017</b>	—	<b>\$1</b>	<b>\$773,385</b>	<b>\$1,143,556</b>	<b>(\$9,005)</b>	<b>\$1,907,937</b>
Net loss prior to organizational transactions	—	—	—	(61,050)	—	(61,050)
Total other comprehensive income	—	—	—	—	1,123	1,123
Effect of organizational transactions	\$2,746,797	(1)	(773,385)	(1,082,506)	—	\$890,905
<b>BALANCES, MARCH 31, 2017</b>	<b>\$2,746,797</b>	—	—	—	<b>(\$7,882)</b>	<b>\$2,738,915</b>
<b>BALANCES, JANUARY 1, 2018</b>	<b>\$2,961,215</b>	—	—	—	<b>(\$5,006)</b>	<b>\$2,956,209</b>
Net income	69,734	—	—	—	—	69,734
Total other comprehensive income	—	—	—	—	1,421	1,421
<b>BALANCES, MARCH 31, 2018</b>	<b>\$3,030,949</b>	—	—	—	<b>(\$3,585)</b>	<b>\$3,027,364</b>

See Notes to Condensed Consolidated Financial Statements

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

<i>(In Thousands)</i>	Three Months Ended March 31,	
	2018	2017
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$69,734	\$829,856
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	82,448	80,431
Unrealized gain on non-hedging derivative instruments	(12,971)	(8,904)
Unrealized loss on foreign currency adjustment of debt financings	12,317	9,271
Amortization of lease incentives and premiums, net	5,395	5,049
Amortization of debt acquisition costs and original issuance discounts	4,455	4,458
Gain on sale of flight equipment	(2,472)	(7,169)
Earnings from equity method investments	(2,251)	(1,204)
Non-hedging derivative instrument settlements	1,400	1,336
Deferred income taxes	623	(875,873)
Maintenance reserves, security deposits and lease incentives included in earnings	(583)	(11,515)
Asset impairment	492	125,149
Other operating activities, net	(65)	(784)
Changes in operating assets and liabilities:		
Accounts payable, accrued expenses and other liabilities	16,413	14,788
Other assets, net	(10,145)	(11,241)
Equity method investments	7,502	—
Deferred income	2,168	(415)
Lease incentives	(201)	(1,496)
<b>NET CASH AND RESTRICTED CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>174,259</b>	<b>151,737</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of flight equipment and related assets	(287,913)	(169,879)
Proceeds from sale of flight equipment	176,555	135,542
Prepayments on flight equipment	(140,074)	(234,548)
Distributions from equity method investments	15,236	—
Capitalized interest on prepayments for flight equipment	(10,823)	(6,650)
Payments on non-hedging derivative instruments	(1,767)	(1,673)
Collections on investment in finance leases, net	5,109	1,956
Receipts from non-hedging derivative instruments	367	337
Other investing activities, net	—	(898)
<b>NET CASH AND RESTRICTED CASH USED IN INVESTING ACTIVITIES</b>	<b>(243,310)</b>	<b>(275,813)</b>

(Continued)

See Notes to Condensed Consolidated Financial Statements

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

<i>(In Thousands)</i>	Three Months Ended March 31,	
	2018	2017
<i>(Continued)</i>		
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from (repayment of) unsecured revolving credit facilities, net	\$373,000	(\$891,000)
Repayment of debt financings	(339,215)	(57,639)
Proceeds from debt financings	2,232	990,973
Receipts of maintenance reserves	44,480	37,946
Payments of maintenance reserves	(14,204)	(2,534)
Receipts of security deposits	6,879	6,118
Payments of security deposits	(1,720)	—
Other financing activities, net	(9)	(1,953)
<b>NET CASH AND RESTRICTED CASH PROVIDED BY FINANCING ACTIVITIES</b>	<b>71,443</b>	<b>81,911</b>
Net change in cash and cash equivalents and restricted cash	2,392	(42,165)
Cash and cash equivalents and restricted cash, beginning of period	373,043	313,427
<b>CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, END OF PERIOD</b>	<b>\$375,435</b>	<b>\$271,262</b>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Interest paid, net of capitalized interest	\$27,647	\$16,589
Security deposits and maintenance reserves settled in sale of flight equipment	\$5,281	\$32,323
Non cash transfer from prepayments on flight equipment to flight equipment held for lease, net	\$197,645	—

See Notes to Condensed Consolidated Financial Statements

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

**1. ORGANIZATION**

Aviation Capital Group LLC, a Delaware limited liability company (ACG LLC), together with its subsidiaries (collectively ACG, we, us, our) is a full service aircraft asset manager. Our business consists primarily of the acquisition, disposition and leasing of commercial jet aircraft, and our principal activity is to act as an owner and lessor of commercial jet aircraft subject to operating leases. We also provide certain asset management services for third parties. Our lessee customers are primarily commercial airlines operating across the globe.

ACG LLC is an indirect subsidiary of Pacific Life Insurance Company (Pacific Life), a wholly owned subsidiary of Pacific LifeCorp (LifeCorp). Pacific Life Aviation Holdings LLC (PLAH), a wholly owned subsidiary of Pacific Life, owns 79% of the membership interests in ACG LLC. TC Skyward Aviation U.S., Inc. (TCSA), a Delaware corporation and direct subsidiary of Tokyo Century Corporation (Tokyo Century), a Japanese corporation, owns 20% of the membership interests in ACG LLC. Aviation Capital Group Holdings, Inc. (ACGHI), a wholly owned subsidiary of PLAH, owns 1% of the membership interests in ACG LLC and is the managing member of ACG LLC. TCSA owns one share of the outstanding common stock of ACGHI.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**BASIS OF PRESENTATION AND PRINCIPLES OF CONSOLIDATION**

The accompanying condensed consolidated financial statements (consolidated financial statements) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim reporting. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The information presented reflects all adjustments, consisting of normal recurring adjustments that, in the opinion of management, are necessary to present fairly the consolidated financial statements for the periods indicated. Results of operations for the interim periods presented are not necessarily indicative of the results of operations for the full year. The condensed consolidated balance sheet as of December 31, 2017 was derived from the audited consolidated financial statements as of December 31, 2017. Therefore, the information included in these consolidated financial statements should be read in conjunction with our audited consolidated financial statements as of and for the year ended December 31, 2017.

Our consolidated financial statements include the accounts of all entities in which we have a controlling financial interest, including the accounts of any variable interest entity (VIE) in which we have a controlling financial interest and thus deemed to be the primary beneficiary.

All intercompany transactions and balances have been eliminated in consolidation.

We manage, operate and present our business as a single segment.

Certain reclassifications have been made in the presentation of the 2017 condensed consolidated statements of cash flow to conform to the 2018 presentation.

We have evaluated events subsequent to March 31, 2018 and through May 16, 2018, the date these consolidated financial statements were available to be issued, and have concluded that except for the items disclosed in Notes 10 and 12, no events or transactions have occurred subsequent to March 31, 2018 that require consideration as adjustments to, or disclosures in, the consolidated financial statements.



## USE OF ESTIMATES

The preparation of financial statements in conformity with U.S. GAAP requires that we make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. While we believe that the estimates and related assumptions used in the preparation of the consolidated financial statements are reasonable, actual results could differ from those estimates. The use of estimates is or could be a significant factor affecting the reported carrying values of flight equipment, acquired contractual rights, lease incentives, deferred income taxes, accruals and reserves. In developing these estimates, we are required to make subjective and complex decisions that are inherently uncertain and subject to material changes as facts and circumstances change.

## RECENT ACCOUNTING PRONOUNCEMENTS ADOPTED

In January 2017, the Financial Accounting Standards Board (FASB) issued new guidance on business combinations, Accounting Standards Update (ASU) 2017-01. The guidance clarifies the definition of a business and provides guidance to determine when a set of assets and activities is a business. We adopted this ASU on January 1, 2018 and it did not have an impact on our consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, which changes the presentation of restricted cash on the statement of cash flows. Restricted cash will be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. We adopted this ASU retrospectively on January 1, 2018 and it resulted in an increase of \$5.8 million in net cash and restricted cash provided by financing activities for the three months ended March 31, 2017 related to reclassifying the changes in our restricted cash balance from financing activities within the condensed consolidated statements of cash flows.

In August 2016, the FASB issued ASU 2016-15, which provides guidance on how certain cash receipts and cash payments are to be presented and classified in the statement of cash flows. We adopted this ASU on January 1, 2018 and it did not have an impact on our consolidated financial statements.

## FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

In August 2017, the FASB issued ASU 2017-12 which targeted improvements to accounting for hedging activities. The amended guidance objective is to improve the financial reporting of hedging relationships to better portray the economic results of a Company's risk management activities in its financial statements and make certain targeted improvements to simplify the application of the hedge accounting guidance. It is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Upon adoption, cash flow and net investment hedges will require a cumulative-effect adjustment related to eliminating the separate measurement of ineffectiveness to accumulated other comprehensive income (AOCI) with a corresponding adjustment to the beginning balance of retained earnings. The amended presentations and disclosure guidance is required only prospectively. Early adoption is permitted. We are currently evaluating the impact of this guidance on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, which primarily amends existing leasing guidance related to a lessee's accounting for operating leases. According to the guidance, accounting for leases by lessors would remain generally unchanged from the current existing concepts. We will adopt this guidance by the required adoption date for private companies of January 1, 2020. We are currently in the process of evaluating the impact of this guidance on our consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, which amends certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The new guidance changes the current accounting guidance related to (i) the classification and measurement of certain equity investments, (ii) the presentation of changes in the fair value of financial liabilities measured under the fair value option that are due to instrument-specific credit risk, and (iii) certain disclosures associated with the fair value of financial instruments. We will adopt this guidance by the required adoption date for private companies of January 1, 2019. We are currently in the process of evaluating the impact of this guidance on our consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, which supersedes most of the current revenue recognition requirements. The guidance requires entities to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. We will adopt this guidance by the required adoption date for private companies of January 1, 2019. We are currently in the process of evaluating the impact of this guidance on our consolidated financial statements.

### 3. FLIGHT EQUIPMENT HELD FOR LEASE, NET

The following table presents the components of flight equipment held for lease, net (*In Thousands*):

	March 31, 2018	December 31, 2017
Cost	\$9,438,450	\$9,088,012
Less: accumulated depreciation	(1,743,819)	(1,663,785)
Flight equipment held for lease, net	<u>\$7,694,631</u>	<u>\$7,424,227</u>

As of March 31, 2018 and December 31, 2017, included in flight equipment held for lease, net is \$160.0 million and \$164.3 million, respectively, of net aircraft maintenance right assets.

As of March 31, 2018 and December 31, 2017, flight equipment held for lease with carrying value of \$1,610.3 million and \$1,627.2 million, respectively, were pledged as collateral for certain secured debt financings (Note 10).

As of March 31, 2018, we did not have any aircraft not subject to a signed lease or sales commitment.

The following table presents, by year, the future minimum lease rentals we are due under operating leases as of March 31, 2018 (*In Thousands*):

Twelve months ended March 31:	
2019	\$893,016
2020	849,343
2021	748,578
2022	664,443
2023	557,616
Thereafter	<u>1,486,490</u>
Total	<u>\$5,199,486</u>

Included in the table above are future lease rentals of \$127.6 million related to six aircraft we lease from third parties and sublease to airlines pursuant to subleases with maturity dates ranging from 2021 to 2024. During the three months ended March 31, 2018 and 2017, the operating lease revenue we received from the subleases related to these aircraft was \$6.8 million. We sold these aircraft to third parties and subsequently leased them back under operating leases with maturity dates ranging from 2023 to 2025. We hold fixed price purchase options exercisable for each of the six operating leases arising from these sale-leaseback transactions. The following table presents our aggregate minimum future lease commitments on these operating leases (*In Thousands*):

Twelve months ended March 31:	
2019	\$20,248
2020	16,722
2021	35,504
2022	28,341
2023	16,552
Thereafter	<u>12,551</u>
Total	<u>\$129,918</u>

#### 4. ASSETS HELD FOR SALE

Assets held for sale consists of flight equipment and the lease-related assets of that aircraft that are part of a sale transaction. Assets held for sale totaled \$361.1 million and \$410.1 million as of March 31, 2018 and December 31, 2017, respectively. Assets held for sale are valued at the lower of carrying value or fair value less costs to sell. We cease recognition of depreciation and amortization expense on all related assets upon transfer to assets held for sale.

When we record assets held for sale at fair value less costs to sell and the amount is less than our carrying value, we record an asset impairment in our condensed consolidated statements of income.

#### 5. INVESTMENT IN FINANCE LEASES, NET

As of March 31, 2018, our investment in finance leases represents 22 aircraft on lease to five customers, with 75% of the carrying value leased to customers based in the U.S. and 17% of the carrying value leased to customers based in Russia. The following table presents the components of investment in finance leases, net (*In Thousands*):

	March 31, 2018	December 31, 2017
Total future minimum lease payments	\$357,614	\$369,111
Less: unearned income	(127,219)	(133,327)
Estimated residual value (unguaranteed)	96,870	96,864
Investment in finance leases, net	<u>\$327,265</u>	<u>\$332,648</u>

The following table presents, by year, the future minimum lease payments we are due on finance leases (*In Thousands*):

Twelve months ended March 31:

2019	\$71,420
2020	39,062
2021	38,422
2022	38,222
2023	37,735
Thereafter	132,753
Total	<u>\$357,614</u>

## 6. GEOGRAPHIC CONCENTRATION

We operated over 87% of our aircraft portfolio, which consists of flight equipment held for lease, net and assets held for sale, in markets outside the U.S. as of March 31, 2018 and December 31, 2017. The following table presents the global concentration of our aircraft portfolio, based on the lessee's location, measured at net book value of flight equipment held for lease and assets held for sale (*Dollars in Thousands*):

	March 31, 2018		December 31, 2017	
	Net Book Value	Percent of Total	Net Book Value	Percent of Total
Region:				
Asia Pacific (excluding China and South Asia)	\$1,879,169	23.3%	\$1,986,687	25.4%
Europe	1,490,051	18.5%	1,318,133	16.8%
Central and South America	1,474,119	18.3%	1,330,815	17.0%
North America	1,208,624	15.0%	1,184,201	15.1%
China	1,028,696	12.8%	1,038,411	13.3%
South Asia	453,611	5.6%	458,028	5.8%
Middle East and Africa	436,082	5.4%	300,834	3.8%
Sub-total	7,970,352	98.9%	7,617,109	97.2%
Aircraft off-lease subject to a signed lease or sales commitment	85,372	1.1%	217,191	2.8%
Total	\$8,055,724	100.0%	\$7,834,300	100.0%

The following table presents the global concentration of our operating lease revenue, based on the lessee's location of record during the three months ended March 31, 2018 and 2017 (*Dollars in Thousands*):

	Three months ended March 31,			
	2018		2017	
	Operating Lease Revenue	Percent of Total	Operating Lease Revenue	Percent of Total
Region:				
Asia Pacific (excluding China and South Asia)	\$53,028	24.1%	\$45,046	21.2%
Europe	39,759	18.0%	45,676	21.5%
North America	39,411	17.9%	35,935	16.9%
Central and South America	38,364	17.4%	38,798	18.3%
China	27,461	12.5%	23,857	11.2%
South Asia	13,319	6.0%	13,307	6.3%
Middle East and Africa	9,026	4.1%	9,794	4.6%
Total	\$220,368	100.0%	\$212,413	100.0%

For the three months ended March 31, 2018 and 2017, no individual lessee accounted for more than 10% of our operating lease revenue. For the three months ended March 31, 2018 and 2017, no country accounted for more than 10% of our operating lease revenue except the U.S. and China.

## 7. VARIABLE INTEREST ENTITIES

### FINANCING STRUCTURES

In connection with certain of our financing structures, we have participated in the design and formation of certain legal entities that we consolidate into our consolidated financial statements. The purpose of these legal entities is to enable our lenders under these financing structures to perfect their security interest in certain aircraft that secure the related debt financings.

These legal entities have entered into loans with various third parties and financial institutions that are primarily guaranteed by us and supported by secondary guarantees from either the Export-Import Bank of the United States (Ex-Im) or the export credit agencies of the United Kingdom, France and/or Germany (ECA) (collectively Export Credit Agencies). These legal entities use the proceeds from these loans to purchase aircraft. The aircraft secure the loans and are leased, pursuant to capital leases, to us. The loans are recourse to the general credit of ACG through the guarantee that is in place.

Some of these legal entities are considered VIEs because they do not have sufficient equity at risk. Additionally, we bear significant risk of loss and participate in gains through the leases and have the power to direct the activities that most significantly impact the economic performance of these legal entities. Therefore, we have determined we are the primary beneficiary of these VIEs and consolidate them into our consolidated financial statements.

The net book value of the aircraft owned by the legal entities that are considered VIEs as of March 31, 2018 and December 31, 2017, totaled \$1,381.4 million and \$1,395.7 million, respectively, and is included in flight equipment held for lease, net (Note 3). In addition, as of March 31, 2018 and December 31, 2017, the debt financing associated with these legal entities totaled \$660.7 million and \$692.6 million, respectively, and is included in debt financings, net (Note 10).

### BACL and BAML

In February 2016, we established two separate joint ventures, Bauhinia Aviation Capital Limited (BACL) and Bauhinia Aviation Management Limited (BAML). BACL was established with two third party investors for the purpose of investing in the purchasing, leasing and selling of commercial aircraft. We owned 20% of the equity of BACL and our subsidiary, ACG Aircraft Leasing Ireland Ltd. (AALIL), acted as the servicer for aircraft owned by BACL. BACL was not consolidated because we were not the primary beneficiary since we did not have the obligation to absorb losses/benefits that could potentially be significant to BACL or a controlling financial interest. As of March 31, 2018 and December 31, 2017, the carrying amount and maximum exposure to loss related to BACL was \$0 and \$14.5 million, respectively, which is included in equity method investments.

BAML was established with a separate third party investor for the purpose of providing management services for BACL. We own 50% of the equity of BAML. BAML is not consolidated because we are not the primary beneficiary since we do not have the obligation to absorb the losses/benefits that could potentially be significant to BAML or a controlling financial interest. As of March 31, 2018 and December 31, 2017, the carrying amount and maximum exposure to loss related to BAML was \$0.7 million, which was included in equity method investments.

In January 2018, we sold our equity interest in BACL and AALIL ceased acting as servicer. In connection with the sale of our equity interest in BACL, BAML ceased providing management services for BACL.

## 8. FAIR VALUE

### ASSETS AND LIABILITIES MEASURED AT FAIR VALUE ON A RECURRING BASIS

Assets and liabilities measured at fair value are classified in their entirety based on the lowest level of input that is significant to their fair value measurement. As of March 31, 2018 and December 31, 2017, we did not have any Level 3 assets or liabilities that we measured at fair value on a recurring basis. The following table presents the assets and liabilities as of March 31, 2018 and December 31, 2017 that we measured at fair value on a recurring basis by level in the fair value hierarchy (*In Thousands*):

	March 31, 2018			December 31, 2017		
	Assets	Liabilities	Total	Assets	Liabilities	Total
Level 2:						
Derivative financial instruments at fair value, net	\$13,501	(\$3,920)	\$9,581	\$1,006	(\$5,690)	(\$4,684)

The fair value of our interest rate swaps, an interest rate cap and foreign currency swap contracts (collectively Derivative Financial Instruments) (Note 9) are determined using market standard valuation methodologies using mid-market inputs that are observable in the market or that can be derived principally from or corroborated by observable market data (Level 2 in the fair value hierarchy) available to us as of March 31, 2018 and December 31, 2017. The pricing models utilize, among other things, interest swap rates, interest rate volatility, and foreign currency forward and spot rates, as applicable. Analysis of the derivative valuations is performed, which includes both quantitative and qualitative analyses. Examples of procedures performed include, but are not limited to, review of internally calculated valuations and comparison to external broker valuations for reasonableness, review of pricing statistics and trends, analysis of the impacts of changes in the market environment, and review of changes in the market value for each derivative by risk managers and accountants. Based on the experience and financial strength of our counterparty, we determined nonperformance risk to be immaterial as of March 31, 2018 and December 31, 2017.

### ASSETS AND LIABILITIES MEASURED AT FAIR VALUE ON A NONRECURRING BASIS

We measure the fair value of our aircraft, and acquired aircraft contractual rights on a non-recurring basis, when events or changes to circumstances indicate that the carrying amounts of the assets may not be recoverable.

For assets held for sale and certain flight equipment held for lease, net or investment in finance leases, net (that were previously held for sale), the fair value measurement is based on the estimated sales price, less selling costs (Level 2 inputs). For flight equipment held for lease, net, and acquired aircraft contractual rights the fair value measurements are based on the present value of the future cash flows (i.e., an income approach) that uses Level 3 inputs.

The following table presents assets impaired to fair value (as measured at the time of the adjustment) on a non-recurring basis during the year and still held as of March 31, 2018 and December 31, 2017, respectively (*In Thousands*):

	March 31, 2018		December 31, 2017	
	Level 2	Level 3	Level 2 (a)	Level 3 (b)
Flight equipment held for lease, net	\$75,348	—	\$18,161	\$15,802
Assets held for sale	—	—	122,720	—
Investment in finance leases, net	—	—	52,286	—
Total	\$75,348	—	\$193,167	\$15,802

(a) Included in flight equipment held for lease, net, is \$18,161 measured during the year ended December 31, 2017. Included in investment in finance leases, net, is \$52,286 measured during the year ended December 31, 2017.

(b) Included in flight equipment held for lease, net, is \$7,994 measured during the year ended December 31, 2017.

## FLIGHT EQUIPMENT HELD FOR LEASE, NET

The income approach is used to measure the fair value of flight equipment held for lease, net. The key inputs to the income approach include the current contractual lease payments, the projected future lease payments extended to the end of the aircraft's estimated holding period in its highest and best use configuration, estimated disposition value less selling costs, and the discount rate.

The current contractual lease payments are based on in-force lease rates. The projected future lease payments are based on the aircraft's type, age, configuration, current contracted lease rates for similar aircraft, industry trends, and the estimated holding period. We generally assume a 25-year estimated economic useful life for aircraft. Shorter holding periods may be used based on our assessment of the continued marketability of certain aircraft types or when a potential sale of an individual aircraft has been identified, or is likely. In the case of a potential sale, the holding period is based on the estimated sale date. The disposition value reflects an estimated residual value or estimated sales price less selling costs and is generally estimated based on aircraft type and condition. The estimated cash flows are then discounted to present value.

During the three months ended March 31, 2018, we made no changes to the valuation techniques used in the fair value measurement of the assets and liabilities discussed above.

## 9. DERIVATIVE FINANCIAL INSTRUMENTS AT FAIR VALUE, NET

The objective of our hedging policy is to adopt a risk averse position with respect to changes in interest rates and foreign currencies.

Our operating lease revenue is generated from rental payments. Rental payments are paid in USD and are generally fixed, but may be fixed or floating with respect to leases entered into in the future. In general, an interest rate or foreign currency exposure with respect to our borrowings arises to the extent that our floating interest and foreign currency obligations do not correlate to the mix of fixed and floating rental payments made in USD for different rental periods. We manage the interest rate and foreign currency exposure with respect to our rental payments and borrowings with Derivative Financial Instruments.

We have entered into a number of interest rate derivatives to hedge the current and future interest rate payments on our variable rate debt financings. Interest rate derivatives are agreements in which a series of interest rate cash flows are exchanged with a third party over a prescribed period. The notional amount on an interest rate derivative is not exchanged. Our interest rate derivatives typically allow us to pay fixed amounts based on fixed interest rates and receive floating amounts based on one-month and three-month London Interbank Offered Rate (LIBOR) to convert our floating rate debt to fixed rate obligations to better match the largely fixed rate cash flows from rental payments.

Furthermore, from time to time we enter into foreign currency swaps that limit exposure to foreign currency fluctuations in connection with the issuance of senior unsecured notes denominated in Japanese yen (JPY) (Note 10). The JPY swap exchanges the three-month JPY LIBOR for the three-month USD LIBOR.

### CASH FLOW HEDGING DERIVATIVE FINANCIAL INSTRUMENTS

As required for all qualifying and highly effective cash flow hedges, the change in the fair value of the interest rate swap contracts was recorded in accumulated other comprehensive loss (AOCL) to the extent effective. During the three months ended March 31, 2018 and 2017, we recorded a pre-tax unrealized gain of \$1.3 million and \$1.4 million, respectively. During the three months ended March 31, 2018 and 2017, all of our hedged forecasted transactions were determined to be probable of occurring. We did not record any ineffectiveness for cash flow hedges during the three months ended March 31, 2018 and 2017. The maximum length of time over which we are hedging our exposure to variability in future cash flows for forecasted transactions does not exceed four years.

Amounts reclassified from AOCL to earnings resulting from the discontinuance of cash flow hedges due to forecasted cash flows that were no longer probable of occurring were zero for the three months ended March 31, 2018 and 2017. Over the next twelve months, we anticipate that \$0.6 million of unrealized losses on derivative instruments in AOCL will be reclassified to earnings. There were no additional deferred realized gains or losses in AOCL as of March 31, 2018 and December 31, 2017.

### CONSOLIDATED FINANCIAL STATEMENT IMPACT

We determine the fair values (Note 8) of our Derivative Financial Instruments using pricing models and inputs that are observable in the market or can be derived principally from or corroborated by observable market data (Level 2 in the fair value hierarchy) available to us as of March 31, 2018 and December 31, 2017.

The following tables present the components of derivative financial instruments at fair value, net (*Dollars in Thousands*):

	March 31, 2018				Fair Value
	Notional	Maturity Date	Pay Rate	Receive Rate	
Interest rate swaps designated as hedging	\$115,460	October 2019 - September 2021	2.7% - 3.5%	1M LIBOR or 3M LIBOR	(\$1,557)
Interest rate swaps not designated as hedging	20,000	September 2019 - July 2033	4.9% - 5.5%	1M LIBOR	(2,363)
Foreign currency swap not designated as hedging	203,427	February 2019	3M USD LIBOR	3M JPY LIBOR	13,501
Derivative financial instruments at fair value, net	<u>\$338,887</u>				<u>\$9,581</u>

	December 31, 2017				Fair Value
	Notional	Maturity Date	Pay Rate	Receive Rate	
Interest rate swaps designated as hedging	\$121,104	October 2019 - September 2021	2.7% - 3.5%	1M LIBOR or 3M LIBOR	(\$2,850)
Interest rate swaps not designated as hedging	20,000	September 2019 - July 2033	4.9% - 5.5%	1M LIBOR	(2,840)
Interest rate cap not designated as hedging	217,000	January 2018	6.5%	1M LIBOR	—
Foreign currency swap not designated as hedging	203,427	February 2019	3M USD LIBOR	3M JPY LIBOR	1,006
Derivative financial instruments at fair value, net	<u>\$561,531</u>				<u>(\$4,684)</u>

The following tables present the pre-tax effect of our Derivative Financial Instruments on the condensed consolidated statements of income excluding net periodic settlements for the three months ended March 31, 2018 and 2017 (*In Thousands*):

	Three months ended March 31, 2018		
	Gain Recognized	Loss Reclassed	Gain Recognized
	In AOCL	from AOCL Into Income (a)	In Income Due To Market Adjustments
Interest rate swaps designated as hedging	\$1,294	—	—
Interest rate swaps not designated as hedging	—	(\$159)	\$476 (b)
Foreign currency swaps not designated as hedging	—	—	12,495
Total gain (loss) on Derivative Financial Instruments	<u>\$1,294</u>	<u>(\$159)</u>	<u>\$12,971</u>

	Three months ended March 31, 2017		
	Gain Recognized	Loss Reclassed	Gain Recognized
	In AOCL	from AOCL Into Income (a)	In Income Due To Market Adjustments
Interest rate swaps designated as hedging	\$1,373	—	—
Interest rate swaps not designated as hedging	—	(\$302)	\$352 (b)
Foreign currency swaps not designated as hedging	—	—	8,552
Total gain (loss) on Derivative Financial Instruments	<u>\$1,373</u>	<u>(\$302)</u>	<u>\$8,904</u>

(a) Represents the amortization of the loss of the de-designated interest rate swaps from AOCL to income.

(b) Represents the mark-to-market adjustments of de-designated interest rate swaps after de-designation.

Credit risk arises from the potential failure of the counterparty to perform according to the terms of the derivative contract. Our exposure to credit risk at any point in time is represented by the fair value of the derivative contract reported as assets. We and the counterparty do not require collateral to support derivative contracts with credit risk. As of March 31, 2018, the counterparty to our derivative contracts was



LifeCorp, which is rated investment grade by Standard and Poor's, Moody's, and Fitch Ratings. A credit valuation analysis was performed for all derivative positions to measure the risk that the counterparty to the transaction will be unable to perform under the contractual terms (nonperformance risk) and the risk was determined to be immaterial as of March 31, 2018.

## 10. DEBT FINANCINGS, NET

The following tables present the components of debt financings, net as of March 31, 2018 and December 31, 2017 (*Dollars in Thousands*):

	March 31, 2018					
	Carrying Amount	Maturity Date	Interest Rate	Type	Interest Period	Currency
Unsecured debt obligations:						
Senior Notes, net	\$4,394,000	April 2018 - November 2027	2.9% - 7.2%	Fixed	Semi-Annual	USD
Revolving Credit Facilities	608,000	December 2019 - April 2022	3.0%	Floating	Monthly	USD
Foreign denominated term loans	217,821	February 2019	0.7%	Floating	Quarterly	JPY
Secured debt obligations:						
Export credit facilities	805,849	December 2018 - November 2024	1.5% - 4.0%	Fixed and Floating	Quarterly	USD
Original issuance discounts	(17,858)					
Debt acquisition costs	(54,162)					
Debt financings, net	<u>\$5,953,650</u>					

	December 31, 2017					
	Carrying Amount	Maturity Date	Interest Rate	Type	Interest Period	Currency
Unsecured debt obligations:						
Senior Notes, net	\$4,694,000	January 2018 - November 2027	2.9% - 7.2%	Fixed	Semi-Annual	USD
Revolving Credit Facilities	235,000	December 2019 - April 2022	2.6%	Floating	Monthly	USD
Foreign denominated term loans	205,504	February 2019	0.7%	Floating	Quarterly	JPY
Secured debt obligations:						
Export credit facilities	842,832	December 2018 - November 2024	1.5% - 3.9%	Fixed and Floating	Quarterly	USD
Original issuance discounts	(18,735)					
Debt acquisition costs	(57,762)					
Debt financings, net	<u>\$5,900,839</u>					

We enter into various senior unsecured financings with third parties. These financings include notes issued in reliance on Rule 144A and Regulation S under the U.S. Securities Act of 1933, as amended, and private placement notes issued to third parties (Senior Notes, net). In May 2018, we issued \$650.0 million of senior notes due 2023 with a fixed interest rate of 3.875%. These notes are recourse to ACG, but not to Pacific Life or LifeCorp.

We enter into various senior unsecured bank credit facilities. We currently are party to two senior unsecured revolving credit facilities (Revolving Credit Facilities) and one foreign denominated term loan. As of March 31, 2018, we have drawn \$608.0 million of the \$1.7 billion capacities on the Revolving Credit Facilities. In April 2018, we increased the capacity of one of our revolving credit facilities from

\$1.5 billion to \$1.6 billion and extended the maturity date from April 2022 to April 2023. These loans are recourse to ACG, but not to Pacific Life or LifeCorp.

We enter into various secured loans guaranteed by Export Credit Agencies, of which portions are financed through VIEs (Note 7). These loans are recourse to ACG, but not to Pacific Life or LifeCorp.

As of March 31, 2018, we were in compliance with all applicable debt covenants.

## 11. COMMITMENTS AND CONTINGENCIES

### CAPITAL COMMITMENTS

As of March 31, 2018, we had commitments to purchase 168 aircraft scheduled for delivery through 2022. In addition, we have a contingent commitment to purchase an additional three aircraft which are not included in the table below. All of these commitments arise from fixed price purchase agreements with Boeing, Airbus and other third parties, and may include escalation provisions. The manufacturers have informed us to expect delivery delays relating to certain aircraft scheduled for delivery in 2018 and 2019. The anticipated delays have been reflected in our commitment schedules below; however, there remains potential of further delivery delays not currently reflected in the schedules below.

The following table presents the estimated remaining payments for the purchase of these aircraft (including adjustments for certain contractual escalation provisions) (*In Thousands*):

Twelve months ended March 31:

2019	\$1,619,007
2020	2,136,156
2021	2,063,811
2022	1,721,208
2023	588,158
Total	<u>\$8,128,340</u>

As of March 31, 2018, deposits made related to these agreements totaled \$1.0 billion and are included in prepayments on flight equipment.

### GENERAL

In the ordinary course of business, as part of contractual agreements, we provide certain indemnifications related to debt financings, aircraft acquisitions, aircraft dispositions, and other transactions. Historically we have not made payments for these types of indemnifications. There are currently no indemnifications from which a probable and reasonably estimable loss could arise. Therefore, as of March 31, 2018 and December 31, 2017, we have no related liabilities to disclose.

In the ordinary course of our business, we are a party to various legal proceedings, claims and litigation we believe are incidental to the operation of our business. Typically, these claims relate to incidents involving our aircraft and claims that involve the existence or breach of a lease, sale, or purchase contract. We regularly review the possible outcome of such legal actions, and accrue for such legal actions at the time a loss is probable and the amount of the loss can be estimated. We also review all applicable indemnities and insurance coverage. Based on information currently available, we believe the potential outcome of these claims, and any reasonably possible losses exceeding amounts already recognized on an aggregated basis, are immaterial to our consolidated financial statements.

## 12. MEMBERS' EQUITY

As of March 31, 2018, PLAH owns 79% of our limited liability company interests, TCSA owns 20% of our limited liability company interests and ACGHI owns 1% of our limited liability company interests. In April 2018, we received a payment of \$4.8 million from TCSA for TCSA's purchase of 20% of our limited liability company interests representing the remaining amount owed to PLAH following the final calculation of the purchase price, and we immediately distributed the funds to PLAH.

### **13. INCOME TAXES**

Our 2018 annual effective tax rate is 0.8% based on our expected tax expense and projected income for 2018. As a result of being a limited liability company, we are taxed as a partnership for U.S. income tax purposes, and not subject to U.S. federal or state income taxes. Therefore, our annual effective tax rate is primarily driven by ACG Singapore tax expense, as our Singapore operations continue to be held by entities subject to tax.

The effective tax rate for the three months ended March 31, 2017 differs from the statutory rate due to the effect of our conversion to a limited liability company, permanent differences and the impact of expected annual foreign income or loss subject to lower statutory rates.

### **14. RELATED PARTY TRANSACTIONS**

For the three months ended March 31, 2018 and 2017, we reimbursed Pacific Life \$16.8 million and \$22.3 million, respectively, for expenses Pacific Life incurred on our behalf, predominantly for the payment of employee compensation and benefits.

As of March 31, 2018, we had a liability to Pacific Mutual Holding Company, LifeCorp's parent company, and Pacific Life totaling \$8.9 million, which is included in accounts payable, accrued expenses and other liabilities.

In February 2018, we entered into a three-year servicing agreement with Tokyo Century to provide certain aircraft related management services for specified aircraft in Tokyo Century's fleet, and we are entitled to receive fees for these services.