

**AVIATION CAPITAL GROUP LLC  
AND SUBSIDIARIES**

Unaudited Condensed Consolidated Financial Statements  
as of September 30, 2019 and December 31, 2018 and for the  
nine months ended September 30, 2019 and 2018

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

<i>(In Thousands)</i>	September 30, 2019	December 31, 2018
<b>ASSETS</b>		
Cash and cash equivalents	\$156,390	\$460,944
Restricted cash	191,265	199,262
Flight equipment held for lease, net	9,668,821	8,781,577
Assets held for sale	85,236	234,784
Prepayments on flight equipment	1,230,784	1,284,305
Investment in finance leases, net	221,079	233,765
Other assets, net	150,569	122,178
<b>TOTAL ASSETS</b>	<b>\$11,704,144</b>	<b>\$11,316,815</b>
<b>LIABILITIES AND EQUITY</b>		
Liabilities:		
Accounts payable, accrued expenses and other liabilities	\$233,987	\$171,375
Debt financings, net	6,973,261	7,029,642
Maintenance reserves	739,738	683,538
Security deposits	166,184	144,317
Deferred income	63,100	63,253
<b>TOTAL LIABILITIES</b>	<b>8,176,270</b>	<b>8,092,125</b>
Commitments and contingencies (Note 10)		
Equity:		
Members' equity	3,527,874	3,227,146
Accumulated other comprehensive loss	—	(2,456)
<b>TOTAL EQUITY</b>	<b>3,527,874</b>	<b>3,224,690</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$11,704,144</b>	<b>\$11,316,815</b>

See Notes to Condensed Consolidated Financial Statements

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

<i>(In Thousands)</i>	Nine Months Ended September 30,	
	2019	2018
<b>REVENUES</b>		
Operating lease revenue	\$755,501	\$691,450
Amortization of lease incentives and premiums, net	(15,635)	(15,384)
Gain on sale of flight equipment, net	23,703	19,480
Maintenance revenue	18,863	—
Other income	60,605	43,210
<b>TOTAL REVENUES</b>	<b>843,037</b>	<b>738,756</b>
<b>EXPENSES</b>		
Depreciation	309,282	257,755
Interest, net	220,151	181,076
Asset impairment	115,212	3,511
Selling, general and administrative	97,696	78,270
<b>TOTAL EXPENSES</b>	<b>742,341</b>	<b>520,612</b>
Income before (benefit from) provision for income taxes and (loss) earnings from equity method investments	100,696	218,144
(Benefit from) provision for income taxes	(207)	2,310
(Loss) earnings from equity method investments	(175)	3,710
<b>NET INCOME</b>	<b>\$100,728</b>	<b>\$219,544</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>	Nine Months Ended September 30,	
	2019	2018
<b>NET INCOME</b>	\$100,728	\$219,544
Other comprehensive income:		
Amortization into earnings from accumulated other comprehensive loss for terminated cash flow hedges, net of taxes of \$192 and zero	2,249	—
Amortization into earnings from accumulated other comprehensive loss for de-designated hedges (included in interest, net)	477	477
Unrealized (loss) gain on interest rate swap contracts, net of taxes of \$42 and \$72 (included in interest, net)	(270)	2,191
<b>COMPREHENSIVE INCOME</b>	\$103,184	\$222,212

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	Accumulated Other Comprehensive (Loss) Income	Total Equity
<b>BALANCES, JANUARY 1, 2018</b>	<b>\$2,961,215</b>	<b>(\$5,006)</b>	<b>\$2,956,209</b>
Net income	219,544	—	219,544
Other comprehensive income	—	2,668	2,668
<b>BALANCES, SEPTEMBER 30, 2018</b>	<b>\$3,180,759</b>	<b>(\$2,338)</b>	<b>\$3,178,421</b>
<b>BALANCES, JANUARY 1, 2019</b>	<b>\$3,227,146</b>	<b>(\$2,456)</b>	<b>\$3,224,690</b>
Capital contribution from TCSA	200,000	—	200,000
Net income	100,728	—	100,728
Other comprehensive income	—	2,456	2,456
<b>BALANCES, SEPTEMBER 30, 2019</b>	<b>\$3,527,874</b>	<b>—</b>	<b>\$3,527,874</b>

See Notes to Condensed Consolidated Financial Statements

The abbreviation TCSA means TC Skyward Aviation U.S., Inc.

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

<i>(In Thousands)</i>	Nine Months Ended September 30,	
	2019	2018
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$100,728	\$219,544
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	309,282	257,755
Amortization of lease incentives and premiums, net	15,635	15,384
Amortization of debt acquisition costs and original issuance discounts	16,163	14,197
Maintenance reserves, security deposits and lease incentives included in earnings	(18,664)	(583)
Asset impairment	115,212	3,511
Gain on sale of flight equipment, net	(23,703)	(19,480)
Other operating activities, net	3,743	837
Change in operating assets and liabilities	(28,619)	9,635
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>489,777</b>	<b>500,800</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of flight equipment and related assets	(1,008,094)	(1,032,974)
Receipts from non-hedging derivative financial instruments	209,316	1,053
Payments on non-hedging derivative financial instruments	(208,491)	(5,902)
Prepayments on flight equipment	(199,237)	(452,835)
Capitalized interest on prepayments on flight equipment	(28,404)	(30,373)
Proceeds from sale of flight equipment and related assets	167,571	348,486
Other investing activities, net	14,401	32,024
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(1,052,938)</b>	<b>(1,140,521)</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>	Nine Months Ended September 30,	
<i>(Continued)</i>	2019	2018
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from debt financings	\$4,368	\$1,732,492
Repayment of debt financings	(348,950)	(1,259,990)
Proceeds from revolving credit facilities and commercial paper, net	274,000	120,000
Capital contribution from TCSA	200,000	—
Receipts of maintenance reserves	151,389	139,131
Payments of maintenance reserves	(53,529)	(36,407)
Receipts of security deposits	30,657	21,084
Payments of security deposits	(5,802)	(8,143)
Other financing activities, net	(1,523)	(4,979)
<b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b>	<b>250,610</b>	<b>703,188</b>
Net change in cash and cash equivalents and restricted cash	(312,551)	63,467
Cash and cash equivalents and restricted cash, beginning of period	660,206	373,043
<b>CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, END OF PERIOD</b>	<b>\$347,655</b>	<b>\$436,510</b>
<b>RECONCILIATION TO CONDENSED CONSOLIDATED BALANCE SHEETS</b>		
Cash and cash equivalents	\$156,390	\$239,386
Restricted cash	191,265	197,124
<b>CASH AND CASH EQUIVALENTS AND RESTRICTED CASH</b>	<b>\$347,655</b>	<b>\$436,510</b>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Interest paid, net of capitalized interest	\$164,348	\$127,966
Non cash transfer from prepayments on flight equipment to flight equipment held for lease, net	\$285,881	\$359,680

See Notes to Condensed Consolidated Financial Statements

The abbreviation TCSA means TC Skyward Aviation U.S., Inc.

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, or 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 invest in and lease commercial jet aircraft pursuant to operating leases. We also provide certain aircraft asset management services and aircraft financing solutions 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). In March 2019, TC Skyward Aviation U.S., Inc. (TCSA), a Delaware corporation and direct subsidiary of Tokyo Century Corporation (Tokyo Century), a Japanese corporation, contributed \$200.0 million of additional equity capital directly to ACG in exchange for newly issued limited liability company interests, increasing TCSA's total ownership in ACG to approximately 24.5% of the outstanding limited liability company interests in ACG. After giving effect to this investment, Pacific Life Aviation Holdings LLC (PLAH), a wholly owned subsidiary of Pacific Life, owns approximately 74.6% of the limited liability company interests in ACG LLC. Aviation Capital Group Holdings, Inc. (ACGHI), a majority owned subsidiary of PLAH, owns approximately 0.9% of the limited liability company interests in ACG LLC and is the managing member of ACG LLC. TCSA owns one share of the outstanding common stock of ACGHI. In September 2019, PLAH, ACGHI and ACG LLC entered into a Membership Interest Purchase Agreement (Purchase Agreement) with TCSA, pursuant to which TCSA has agreed to purchase all of PLAH's and ACGHI's outstanding limited liability company interests in ACG LLC. Upon the closing of this transaction, TCSA will own 100% of the outstanding limited liability company interests in ACG LLC. At the closing of the transaction, TCSA will also transfer its one share of the outstanding common stock of ACGHI to PLAH. The closing of the transaction is subject to the fulfillment of customary closing conditions contained in the Purchase Agreement, including the receipt of certain regulatory approvals.

**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 fairly state the consolidated financial statements for the periods indicated. Statements of income 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, 2018 was derived from the audited consolidated financial statements as of December 31, 2018. 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, 2018.

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) where we are 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 line items have been combined in the presentation of the 2018 condensed consolidated statements of income and condensed consolidated statements of cash flows to conform to the 2019 presentation.



## 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, 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.

## RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

In 2017, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2017-12, which, together with all subsequent amendments, targets improvements to accounting for hedging activities. The objective of the amended guidance 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. 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 loss (AOCL) with a corresponding adjustment to the beginning balance of members' equity. We adopted this standard on January 1, 2019. The amendments in this guidance did not have a material impact on our consolidated financial statements.

In 2014, the FASB issued ASU 2014-09, which, together with all subsequent amendments, supersedes most of the current revenue recognition guidance. The guidance does not apply to lease contracts with customers. The guidance requires entities to recognize revenue when it transfers control of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additionally, the guidance requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. As the guidance did not apply to lease contracts within the scope of Accounting Standards Codification (ASC) 840 Leases, we evaluated the recognition of gains on sale of flight equipment and components of other income under the scope of the new guidance. Based on our evaluation, the timing and nature of how we recognize revenue related to gain on sale of flight equipment as well as components of other income is consistent under the new guidance. We adopted this standard on January 1, 2019 using the modified retrospective method. The amendments in this guidance did not have a material impact on our consolidated financial statements.

## FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

In 2016, the FASB issued ASU 2016-13, which, together with all subsequent amendments, provides guidance on the measurement of credit losses for certain financial assets. The new guidance replaces the incurred loss impairment methodology with one that reflects expected credit losses. The measurement of expected credit losses should be based on historical loss information, current conditions, and reasonable and supportable forecasts. The guidance also requires enhanced disclosures. The amendments in this guidance are effective for fiscal years beginning after December 15, 2020 and interim periods within those fiscal years with a cumulative-effect adjustment to members' equity under a modified-retrospective approach. Early adoption is permitted. We are currently evaluating the impact of this guidance on our consolidated financial statements.

In 2016, the FASB issued ASU 2016-02, which, together with all subsequent amendments, primarily amends existing leasing guidance related to a lessee's accounting for operating leases. The new guidance requires a lessee to recognize assets and liabilities for leases with lease terms of more than 12 months. Consistent with current guidance, leases would be classified as finance or operating leases. However, unlike current guidance, the new guidance will require both types of leases to be recognized on the condensed consolidated balance sheets by the lessee. Lessor accounting will remain largely unchanged from current guidance except for certain targeted changes. The amendments in this guidance are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted. We are currently evaluating the impact of this guidance on our consolidated financial statements. We do not expect the amendments in this guidance to have a material impact 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*):

	September 30, 2019	December 31, 2018
Cost of flight equipment held for lease	\$11,889,884	\$10,765,060
Less: accumulated depreciation	(2,221,063)	(1,983,483)
Flight equipment held for lease, net	<u>\$9,668,821</u>	<u>\$8,781,577</u>

As of September 30, 2019 and December 31, 2018, maintenance right assets of \$172.0 million and \$166.6 million, respectively, were included in flight equipment held for lease, net.

As of September 30, 2019 and December 31, 2018, flight equipment held for lease, net with carrying values of \$1,282.3 million and \$1,422.3 million, respectively, were pledged as collateral for certain secured debt obligations (Note 9).

During the nine months ended September 30, 2019 and 2018, impairments related to flight equipment held for lease, net and lease acquisition costs were \$114.4 million and \$1.3 million, respectively, and impairments related to assets held for sale were \$0.8 million and \$2.2 million, respectively. Impairments may be derived from maintenance adjusted estimated values, estimated sale prices, or a reduction of estimated future cash flows (Note 7).

The following table presents the future minimum lease rentals we are due under operating leases as of September 30, 2019 (*In Thousands*):

Years Ended December 31:	
Remainder of 2019	\$247,041
2020	950,601
2021	870,642
2022	791,131
2023	676,454
Thereafter	2,649,344
Total	<u>\$6,185,213</u>

Included in the table above are lease rentals we are due relating to five aircraft that we sold to third parties, then leased back under operating leases (the Head Leases), and subsequently leased to airlines (the Sub Leases). During each of the nine months ended September 30, 2019 and 2018, the operating lease revenue we received from the Sub Leases was \$20.3 million. The table above includes future minimum lease rentals related to the Sub Leases of \$72.1 million. The Sub Leases have maturity dates ranging from 2021 to 2024.

During 2019, we held fixed price purchase options under the Head Leases for six aircraft and exercised the fixed price purchase option on two of the six aircraft. The purchase of one aircraft closed in September 2019, and the purchase of the other aircraft is scheduled to close in late 2019. The commitment related to the remaining exercised purchase option is \$28.4 million, which is scheduled to be paid in 2019 and 2020, and is included in the table below. The remaining four Head Leases have maturity dates ranging from 2023 to 2025. The following table includes our aggregate minimum future lease commitments on the Head Leases as of September 30, 2019 (*In Thousands*):

Years Ended December 31:	
Remainder of 2019	\$27,520
2020	31,177
2021	15,556
2022	15,683
2023	14,783
Thereafter	7,171
Total	<u>\$111,890</u>

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

As of September 30, 2019, our investment in finance leases, net, represents 17 aircraft on lease to two customers. As of September 30, 2019 and December 31, 2018, 100% of our investment in finance leases, net, by carrying value were operated in the U.S. The following table presents the components of investment in finance leases, net (*In Thousands*):

	September 30, 2019	December 31, 2018
Total future minimum lease payments	\$231,125	\$255,981
Less: unearned income	(77,590)	(89,743)
Estimated unguaranteed residual value	67,544	67,527
Investment in finance leases, net	<u>\$221,079</u>	<u>\$233,765</u>

The following table presents the future minimum lease payments that we are due under finance leases as of September 30, 2019 (*In Thousands*):

Years Ended December 31:	
Remainder of 2019	\$8,286
2020	33,032
2021	32,882
2022	32,782
2023	32,722
Thereafter	91,421
Total	<u>\$231,125</u>

#### 5. GEOGRAPHIC CONCENTRATION

The following table presents the global concentration of our aircraft portfolio, based on the lessee's location (*Dollars In Thousands*):

	September 30, 2019		December 31, 2018	
	Net Book Value	Percent of Total	Net Book Value	Percent of Total
Region:				
Asia Pacific (excluding China and South Asia)	\$2,272,377	23.3%	\$1,918,546	21.3%
Europe	1,638,585	16.7%	1,591,421	17.7%
China	1,387,237	14.2%	1,219,641	13.5%
Central America, South America and Mexico	1,253,535	12.9%	1,345,297	14.9%
United States and Canada	1,238,413	12.7%	1,201,315	13.3%
Middle East and Africa	769,018	7.9%	629,532	7.0%
South Asia	455,320	4.7%	629,893	7.0%
Sub-total	<u>9,014,485</u>	<u>92.4%</u>	<u>8,535,645</u>	<u>94.7%</u>
Aircraft off-lease subject to a signed lease or sales commitment	410,552	4.2%	175,153	1.9%
Aircraft off-lease not subject to a signed lease or sales commitment	329,020	3.4%	305,563	3.4%
Total	<u>\$9,754,057</u>	<u>100.0%</u>	<u>\$9,016,361</u>	<u>100.0%</u>

As of September 30, 2019 and December 31, 2018, no individual lessee accounted for more than 10% of our aircraft portfolio, which consists of flight equipment held for lease, net and assets held for sale. As of September 30, 2019, no country accounted for more than 10% of our aircraft portfolio, which consists of flight equipment held for lease, net and assets held for sale, except China. As of December 31, 2018, no country accounted for more than 10% of our aircraft portfolio, which consists of flight equipment held for lease, net and assets held for sale, except the U.S. and China.

The following table presents the global concentration of our operating lease revenue, based on the lessee's location, during the nine months ended September 30, 2019 and 2018 (*Dollars In Thousands*):

	Nine Months Ended September 30,			
	2019		2018	
	Lease Revenue	Percent of Total	Lease Revenue	Percent of Total
Asia Pacific (excluding China and South Asia)	\$172,785	22.9%	\$155,278	22.5%
Europe	159,485	21.1%	141,659	20.5%
United States and Canada	118,980	15.7%	114,891	16.6%
Central America, South America and Mexico	109,144	14.4%	124,451	18.0%
China	106,324	14.1%	82,846	12.0%
Middle East and Africa	45,029	6.0%	30,390	4.3%
South Asia	43,754	5.8%	41,935	6.1%
Operating lease revenue	\$755,501	100.0%	\$691,450	100.0%

For the nine months ended September 30, 2019 and 2018, no individual lessee accounted for more than 10% of our operating lease revenue. For the nine months ended September 30, 2019 and 2018, no country accounted for more than 10% of our operating lease revenue except the U.S. and China.

## 6. 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 ACG and supported by secondary guarantees from either the Export-Import Bank of the United States (Ex-Im) or the export credit agencies (ECA) of the United Kingdom, France and/or Germany (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 our general credit through the ACG guarantee that is in place.

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 legal entities that are considered VIEs as of September 30, 2019 and December 31, 2018, totaled \$1,093.5 million and \$1,227.1 million, respectively, and is included in flight equipment held for lease, net (Note 3). In addition, as of September 30, 2019 and December 31, 2018, the debt financings associated with these legal entities totaled \$414.9 million and \$534.4 million, respectively, and are included in debt financings, net (Note 9).

## 7. FAIR VALUE

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. We determine fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

Level 1	Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.
Level 2	Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
Level 3	Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date.

In some cases, the inputs used to measure fair value can fall into different levels of the fair value hierarchy. In such cases, the determination of which category within the fair value hierarchy is appropriate for any given financial instrument is based on the lowest level of input that is significant to the fair value measurement.

The valuation approaches that may be used to measure fair value are as follows:

Market	Uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.
Income	Uses valuation techniques to convert future amounts to a single current amount based on current market expectation about those future amounts.
Cost	Based on the amount that would be required currently to replace the service capacity of an asset (current replacement cost).

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

We record derivative financial instruments, such as interest rate and foreign currency swap contracts (collectively Derivative Financial Instruments), at fair value. Certain Derivative Financial Instruments were subject to master netting agreements, which allowed the netting of derivative assets and liabilities by counterparty in the event of a default under any one contract. Derivative Financial Instruments in a net asset position by counterparty are recorded in other assets, net. Derivative Financial Instruments in a net liability position by counterparty are recorded in accounts payable, accrued expenses and other liabilities.

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. The following table presents Level 2 Derivative Financial Instrument assets and liabilities measured at fair value on a recurring basis, based on counterparty (*In Thousands*):

	September 30, 2019		
	Assets	Liabilities	Total
Third party financial institution	\$2,211	—	\$2,211

  

	December 31, 2018		
	Assets	Liabilities	Total
LifeCorp	\$7,406	(\$2,862)	\$4,544
Third party financial institution	1,040	—	1,040

As of September 30, 2019 and December 31, 2018, we did not have any Level 3 assets or liabilities that we measured at fair value on a recurring basis.

We use Derivative Financial Instruments to manage exposure to changes in interest rates and foreign currencies. The fair value of our Derivative Financial Instruments (Note 8) 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 September 30, 2019 and December 31, 2018. 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,

obtaining third party valuations and reviewing internally calculations 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 counterparties, we determined nonperformance risk to be immaterial as of September 30, 2019 and December 31, 2018.

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

We measure the fair value of our aircraft and related assets when events or changes to circumstances indicate that the carrying amounts of these assets may not be recoverable.

The following table presents assets measured at fair value (at the relevant measurement date) on a non-recurring basis as of September 30, 2019 and December 31, 2018 (*In Thousands*):

	September 30, 2019		December 31, 2018	
	Level 2	Level 3	Level 2	Level 3
Flight equipment held for lease, net	—	\$270,750	—	\$243,680
Assets held for sale	—	—	\$72,139	—
Total	—	\$270,750	\$72,139	\$243,680

The fair value measurements of our aircraft and related assets may be based on the estimated sales price less selling costs (i.e., a market approach) based on Level 2 inputs, maintenance adjusted estimated values (i.e., a market approach) based on Level 3 inputs, or the present value of estimated future cash flows (i.e., an income approach) based on Level 3 inputs. We used the market or income approach for all assets measured at fair value on a non-recurring basis for the nine months ended September 30, 2019, and for the year ended December 31, 2018.

During the nine months ended September 30, 2019 and 2018, impairments related to maintenance right assets and lease acquisition costs were \$9.2 million and zero, respectively. These maintenance right assets and lease acquisition costs were measured at a fair value of zero, as there are no future contractual cash flows due to the termination of the respective leases.

#### LEVEL 3 INPUTS FOR FLIGHT EQUIPMENT HELD FOR LEASE, NET MEASURED AT FAIR VALUE ON A NON-RECURRING BASIS

The key inputs for the income approach include the current contractual lease payments, estimated 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 key inputs to the market approach include maintenance adjusted estimated values.

The current contractual lease payments are based on in-force lease rates. Estimated 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 or longer 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, condition, and contractual terms. The estimated cash flows are then discounted to present value.

For flight equipment held for lease, net that we measured at fair value on a non-recurring basis using Level 3 inputs during the nine months ended September 30, 2019, the following table presents the fair value as of the measurement dates, the valuation technique and the related unobservable inputs (*In Thousands*):

	Fair Value	Valuation Technique	Unobservable Input
Flight equipment held for lease, net	\$270,750	Market Approach	Maintenance Adjusted Estimated Values

During the nine months ended September 30, 2019 and the year ended December 31, 2018, we made no transfers into or out of Level 3 assets, nor did we purchase or issue Level 3 assets or liabilities.

## FINANCIAL ASSETS AND LIABILITIES

Our financial assets and liabilities include cash and cash equivalents, restricted cash, investment in finance leases, net, operating lease receivables, notes and other receivables, Derivative Financial Instruments, accounts payable, accrued expenses and other liabilities, and debt financings, net. Our financial assets and liabilities are carried at amortized cost with the exception of Derivative Financial Instruments which are carried at fair value.

### 8. DERIVATIVE FINANCIAL INSTRUMENTS

The objective of our hedging policy is to mitigate risk with respect to changes in interest rates and foreign currencies.

Our operating lease revenue is generated from rental payments. Rental payments 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 U.S. Dollars (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.

From time to time, we enter into foreign currency swaps that limit our exposure to foreign currency fluctuations in connection with the issuance of term loans denominated in Japanese yen (JPY) (Note 9). The JPY swap exchanges the three-month JPY LIBOR for the three-month USD LIBOR.

At times, we enter into interest rate derivatives to hedge the current and future interest rate payments on our floating 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.

#### 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 were recorded in AOCL. During the nine months ended September 30, 2019 and 2018, we recorded a pre-tax unrealized (loss)/gain of (\$0.2) million and \$2.3 million, respectively.

For the nine months ended September 30, 2019 and 2018, \$2.5 million and zero, respectively, were amortized from AOCL to earnings for terminated and de-designated cash flow hedges. No amounts were 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 for the nine months ended September 30, 2019 and 2018. We had no deferred realized gains or losses in AOCL as of September 30, 2019.

We did not record any ineffectiveness for cash flow hedges during the nine months ended September 30, 2019 and 2018.

#### CONSOLIDATED FINANCIAL STATEMENT IMPACT

We determine the fair values (Note 7) 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 September 30, 2019 and December 31, 2018.

The following tables present our derivative financial instruments (*Dollars In Thousands*):

	September 30, 2019				
	Fair Value	Maturity Date	Pay Rate	Receive Rate	Notional
Foreign currency swaps not designated as hedging	\$2,211	July 2023	3M USD LIBOR	3M JPY LIBOR	\$97,367

		December 31, 2018			
	Fair Value	Maturity Date	Pay Rate	Receive Rate	Notional
Interest rate swaps designated as hedging	(\$849)	October 2019 - September 2021	2.7% - 3.5%	1M LIBOR or 3M LIBOR	\$94,822
Interest rate swaps not designated as hedging	(2,013)	September 2019 - July 2033	4.9% - 5.5%	1M LIBOR	20,000
Foreign currency swaps not designated as hedging	8,446	February 2019 - July 2023	3M USD LIBOR	3M JPY LIBOR	300,795

The following tables present the pre-tax effect of our Derivative Financial Instruments (*In Thousands*):

	Nine Months Ended September 30, 2019		
	Unrealized Loss Recognized In AOCL	Loss Amortized From AOCL Into Income (a)	Unrealized Loss Recognized In Income Due To Market Adjustments
Interest rate swaps designated as hedging	(\$228)	(\$1,077)	—
Interest rate swaps not designated as hedging	—	(1,457)	(\$448) (b)
Foreign currency swaps not designated as hedging	—	—	(6,235)
Unrealized loss on hedging and non-hedging Derivative Financial Instruments	(\$228)	(\$2,534)	(\$6,683)

	Nine Months Ended September 30, 2018		
	Unrealized Gain Recognized In AOCL	Loss Amortized From AOCL Into Income (a)	Unrealized Gain (Loss) Recognized In Income Due To Market Adjustments
Interest rate swaps designated as hedging	\$2,263	—	—
Interest rate swaps not designated as hedging	—	(\$477)	\$982 (b)
Foreign currency swaps not designated as hedging	—	—	(4,229)
Unrealized gain (loss) on hedging and non-hedging Derivative Financial Instruments	\$2,263	(\$477)	(\$3,247)

(a) Represents the amortization of the loss of de-designated interest rate swaps from AOCL to income and the amortization into earnings from AOCL for terminated and de-designated cash flow hedges.

(b) Represents 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. Neither we nor our counterparty requires collateral to support our current derivative contracts with credit risk. As of September 30, 2019, the counterparty to our derivative contracts was rated investment grade by Standard and Poor's, Moody's, and Fitch Ratings. A credit valuation analysis was performed for our derivative position 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 September 30, 2019.

As of September 30, 2019 and December 31, 2018, we had a foreign currency swap not designated as hedging with a fair value asset of \$2.2 million and \$1.0 million, respectively, which contained a termination event clause. Pursuant to the termination event clause, if there is a change in ownership and our financial strength ratings as assigned by certain independent rating agencies fall below a specified level, as defined within the International Swaps and Derivative Association (ISDA) master agreement, the counterparty could terminate the ISDA master agreement with payment due based on the fair value of the underlying derivatives.



## 9. DEBT FINANCINGS, NET

The following tables present the components of debt financings, net, as of September 30, 2019 and December 31, 2018 (*Dollars In Thousands*):

	September 30, 2019					
	Carrying Amount	Maturity Date	Interest Rate	Type	Interest Period	Currency
Unsecured debt obligations:						
Senior Notes	\$5,832,000	April 2020 - November 2027	2.9% - 7.2%	Fixed and Floating	Semi-Annual and Quarterly	USD
Commercial paper	390,000	October 2019 - November 2019	2.3% - 2.8%	Fixed	Various	USD
Term loans	296,926	July 2023	0.3% - 3.3%	Floating	Quarterly	USD and JPY
Revolving Credit Facilities	—	December 2019 - June 2024	—	Floating	Monthly	USD
Secured debt obligations:						
Export Credit Facilities	528,667	August 2020 - November 2024	1.5% - 3.8%	Fixed and Floating	Quarterly	USD
Debt acquisition costs	(50,429)					
Original issuance discounts	(23,903)					
Debt financings, net	<u>\$6,973,261</u>					

	December 31, 2018					
	Carrying Amount	Maturity Date	Interest Rate	Type	Interest Period	Currency
Unsecured debt obligations:						
Senior Notes	\$5,832,000	April 2020 - November 2027	2.9% - 7.2%	Fixed and Floating	Semi-Annual and Quarterly	USD
Term loans	506,509	February 2019 - July 2023	0.3% - 3.4%	Floating	Quarterly	USD and JPY
Commercial paper	96,000	January 2019	2.8% - 2.9%	Fixed	Various	USD
Revolving Credit Facilities	20,000	December 2019 - April 2023	3.6%	Floating	Monthly	USD
Secured debt obligations:						
Export Credit Facilities	664,105	September 2019 - November 2024	1.5% - 4.2%	Fixed and Floating	Quarterly	USD
Debt acquisition costs	(61,490)					
Original issuance discounts	(27,482)					
Debt financings, net	<u>\$7,029,642</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).

We are party to two senior unsecured revolving credit facilities, the 2013 Revolving Credit Facility and the 2019 Revolving Credit Facility (collectively, Revolving Credit Facilities). In June 2019, we amended and restated the 2019 Revolving Credit Facility, which increased the capacity from \$1,640.0 million to \$2,010.0 million and extended the maturity date from April 2023 to June 2024. The 2013 Revolving Credit Facility matures in December 2019 and has total borrowing capacity of \$220.0 million. As of September 30, 2019 we had drawn zero of the \$2,230.0 million aggregate capacity available under the Revolving Credit Facilities. As of December 31, 2018 we had drawn \$20.0 million of the \$1,860.0 million aggregate capacity available under the Revolving Credit Facilities.

We have a \$1.5 billion commercial paper program under which we may issue notes in minimum denominations of \$250.0 thousand for periods ranging from one to 397 days. The 2019 Revolving Credit Facility serves as a backstop facility for our commercial paper program. As of September 30, 2019 and December 31, 2018, we had issued \$390.0 million and \$96.0 million, respectively, of commercial paper.

We enter into various secured loans guaranteed by Export Credit Agencies and ACG (Export Credit Facilities), some of which are financed through VIEs (Note 6).

All of our outstanding debt as of September 30, 2019 is recourse only to ACG, and is not guaranteed by any of ACG's equity holders, including Pacific Life, LifeCorp or Tokyo Century.

As of September 30, 2019 and December 31, 2018, we were in compliance with all applicable debt covenants.

## 10. COMMITMENTS AND CONTINGENCIES

### LEASE COMMITMENTS

We lease office facilities in Newport Beach, California; Bellevue, Washington; Dublin, Ireland; and Singapore under non-cancelable operating leases.

We have lease rental commitments relating to five aircraft we sold to third parties then leased back under operating leases (Note 3).

### CAPITAL COMMITMENTS

As of September 30, 2019, we had commitments to purchase 162 aircraft scheduled for delivery through 2025. 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. Under certain circumstances, we have the right to alter the mix of aircraft types ultimately acquired. The manufacturers have informed us of delivery delays relating to certain aircraft, including as a result of the Boeing MAX situation described below. These delays have been reflected in our commitment schedule below; however, there remains potential of further delivery delays not currently reflected in the schedule below. Our leases contain lessee cancellation clauses related to aircraft delivery delays, typically for delays greater than one year. Our purchase agreements with Boeing and Airbus contain similar clauses.

In March 2019, the Federal Aviation Administration issued an order to suspend operations of all Boeing 737 MAX aircraft in the U.S. and by U.S. aircraft operators. Non-U.S. civil aviation authorities have also issued directives to similar effect. Boeing has suspended deliveries of the Boeing 737 MAX until clearance is granted by the appropriate regulatory authorities. Prior to the grounding, we had delivered seven Boeing 737 MAX aircraft that are currently on lease to four airline customers, and we currently have 97 Boeing 737 MAX aircraft on order. It is uncertain when and under what conditions the Boeing 737 MAX will return to service and when Boeing will resume making deliveries of these aircraft. As a result, we have incurred delays and expect to incur future delays on our scheduled Boeing 737 MAX deliveries. The commitment schedule below reflects our estimate of when the Boeing 737 MAX deliveries will resume.

The following table presents the estimated remaining payments for the purchase of aircraft (including adjustments for certain contractual escalation provisions) as of September 30, 2019 (*In Thousands*):

Years Ended December 31:

Remainder of 2019	\$464,871
2020	1,920,618
2021	2,074,220
2022	1,571,176
2023	774,427
Thereafter	841,522
Total	<u>\$7,646,834</u>

As of September 30, 2019, non-refundable deposits made related to our purchase agreements totaled \$1.1 billion and are included in prepayments on flight equipment.

### GUARANTEES

We have structured, arranged and provided guarantees of the repayment of third-party secured term loans. Such loans were used to finance a portion of the purchase price of new aircraft by third-party airlines. We received upfront fees for our role in the financing transactions. We recorded a portion of the upfront fees as a guarantee liability for our estimated credit loss which is included in accounts

payable, accrued expenses and other liabilities. The remaining portion of the upfront fees related to structuring and arranging the financing transactions were recorded in other income. As of September 30, 2019, the estimated market value of the aircraft pledged as collateral on the loans are greater than the amount guaranteed by ACG.

## 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 September 30, 2019 and December 31, 2018, 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.

## 11. MEMBERS' EQUITY

ACG LLC currently has 105,964 limited liability company interests outstanding, of which 79,000 are held by PLAH, 25,964 are held by TCSA and 1,000 are held by ACGHI. As described in Note 1, TCSA has entered into a Purchase Agreement with PLAH and ACGHI to acquire all of their outstanding limited liability company interests in ACG LLC.

## 12. INCOME TAXES

Our 2019 year to date effective tax rate is (0.2%) based on our expected annual tax expense and projected income for 2019 as adjusted for discrete tax benefits. As a result of being a limited liability company, we are taxed as a partnership for U.S. income tax purposes, and we are not subject to U.S. federal or state income taxes. Therefore, our annual effective tax rate is primarily driven by the operations of our foreign entities that remain subject to tax.

The effective tax rate for the nine months ended September 30, 2019 differs from the statutory rate due to our status as a limited liability company, permanent differences and the impact of expected annual foreign income or loss subject to lower statutory rates.

## 13. RELATED PARTY TRANSACTIONS

For the nine months ended September 30, 2019 and 2018, we reimbursed Pacific Life \$49.6 million and \$41.1 million, respectively, for expenses Pacific Life incurred on our behalf, primarily for the payment of employee compensation and benefits, and other services.

As of September 30, 2019 and December 31, 2018, we had a liability to Pacific Life totaling \$1.4 million, which is included in accounts payable, accrued expenses and other liabilities.

We participate in a defined contribution Retirement Incentive Savings Plan sponsored by Pacific Life, which covers substantially all employees. We match 75% of employee contributions, up to a maximum of 6% of eligible employee compensation up to the IRS maximum allowable amount. For each of the nine months ended September 30, 2019 and 2018, our share of net expenses under this plan, included in selling, general and administrative expense, was \$2.5 million and \$2.4 million, respectively.

We had derivative contracts with LifeCorp as the counterparty. The majority of the settlement payments with LifeCorp are included in receipts from non-hedging derivative financial instruments and payments on non-hedging derivative financial instruments within our condensed consolidated statements of cash flows. As of September 30, 2019, we terminated all our derivative contracts with LifeCorp.

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. For the nine months ended September 30, 2019 and 2018, we received \$2.8 million and \$2.5 million, respectively, in fees for these services, which is included in other income.

#### **14. SUBSEQUENT EVENTS**

We have evaluated events subsequent to September 30, 2019 and through November 12, 2019, the date these consolidated financial statements were available to be issued, and have concluded that, except for the events noted below, no events or transactions have occurred subsequent to September 30, 2019 that require consideration as adjustments to, or disclosures in, the consolidated financial statements.

In October 2019, we entered into an agreement to sell 24 aircraft to MACH 1 Cayman Limited and its subsidiaries (MACH 1), an asset-backed securities platform which will facilitate the sale of aircraft assets to investors. ACG will retain a non-controlling interest in MACH 1 of 9.5% of the outstanding equity. All of the aircraft in MACH 1's portfolio will be managed by ACG.