

Edgar Filing: Aircastle LTD - Form 10-Q

Aircastle LTD  
Form 10-Q  
November 01, 2016

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934

For the quarterly period ended September 30, 2016

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934

For the transition period from            to

Commission File number 001-32959

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AIRCASTLE LIMITED

(Exact name of registrant as specified in its charter)

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Bermuda	98-0444035
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

c/o Aircastle Advisor LLC	06902
300 First Stamford Place, 5 <sup>th</sup> Floor, Stamford, CT	(Zip Code)
(Address of principal executive offices)	
Registrant's telephone number, including area code	(203) 504-1020

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Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
YES  NO

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As of October 28, 2016, there were 78,634,132 outstanding shares of the registrant's common shares, par value \$0.01 per share.

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Aircastle Limited and Subsidiaries  
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## PART I. — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## Aircastle Limited and Subsidiaries

## Consolidated Balance Sheets

(Dollars in thousands, except share data)

	September 30, 2016	December 31, 2015
	(Unaudited)	
<b>ASSETS</b>		
Cash and cash equivalents	\$ 656,247	\$ 155,904
Accounts receivable	5,266	8,566
Restricted cash and cash equivalents	54,000	98,137
Restricted liquidity facility collateral	—	65,000
Flight equipment held for lease, net of accumulated depreciation of \$1,245,447 and \$1,306,024, respectively	6,004,489	5,867,062
Net investment in finance and sales-type leases	265,854	201,211
Unconsolidated equity method investment	67,160	50,377
Other assets	129,840	123,707
Total assets	\$ 7,182,856	\$ 6,569,964
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>LIABILITIES</b>		
Borrowings from secured financings, net of debt issuance costs	\$ 1,261,423	\$ 1,146,238
Borrowings from unsecured financings, net of debt issuance costs	3,286,304	2,894,918
Accounts payable, accrued expenses and other liabilities	144,140	131,058
Lease rentals received in advance	61,095	67,327
Liquidity facility	—	65,000
Security deposits	128,109	115,642
Maintenance payments	516,689	370,281
Total liabilities	5,397,760	4,790,464
Commitments and Contingencies		
<b>SHAREHOLDERS' EQUITY</b>		
Preference shares, \$0.01 par value, 50,000,000 shares authorized, no shares issued and outstanding	—	—
Common shares, \$0.01 par value, 250,000,000 shares authorized, 78,634,133 shares issued and outstanding at September 30, 2016; and 80,232,260 shares issued and outstanding at December 31, 2015	786	802
Additional paid-in capital	1,519,849	1,550,337
Retained earnings	268,601	241,574
Accumulated other comprehensive loss	(4,140)	(13,213)
Total shareholders' equity	1,785,096	1,779,500
Total liabilities and shareholders' equity	\$ 7,182,856	\$ 6,569,964

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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Aircastle Limited and Subsidiaries  
 Consolidated Statements of Income (Loss)  
 (Dollars in thousands, except per share amounts)  
 (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues:				
Lease rental revenue	\$181,975	\$188,038	\$537,670	\$550,023
Finance and sales-type lease revenue	5,354	1,868	13,026	5,352
Amortization of net lease discounts and lease incentives	(521 )	(2,113 )	(5,419 )	(10,288 )
Maintenance revenue	6,829	15,726	20,603	55,148
Total lease revenue	193,637	203,519	565,880	600,235
Other revenue	1,015	8,555	2,425	10,700
Total revenues	194,652	212,074	568,305	610,935
Operating expenses:				
Depreciation	76,201	85,324	227,918	237,538
Interest, net	61,797	60,381	188,490	184,063
Selling, general and administrative (including non-cash share-based payment expense of \$2,059 and \$1,424 for the three months ended and \$5,796 and \$3,981 for the nine months ended September 30, 2016 and 2015, respectively)	15,985	14,032	46,883	42,663
Impairment of aircraft	10,462	78,403	27,185	102,358
Maintenance and other costs	1,834	2,520	5,504	9,126
Total expenses	166,279	240,660	495,980	575,748
Other income (expense):				
Gain (loss) on sale of flight equipment	(73 )	15,679	14,932	43,034
Other	(210 )	70	(136 )	341
Total other income (expense)	(283 )	15,749	14,796	43,375
Income (loss) from continuing operations before income taxes and earnings of unconsolidated equity method investment	28,090	(12,837 )	87,121	78,562
Income tax provision	2,458	2,709	8,782	12,037
Earnings of unconsolidated equity method investment, net of tax	1,805	1,557	5,390	4,563
Net income (loss)	\$27,437	\$(13,989 )	\$83,729	\$71,088
Earnings (loss) per common share — Basic:				
Net income (loss) per share	\$0.35	\$(0.17 )	\$1.06	\$0.88
Earnings (loss) per common share — Diluted:				
Net income (loss) per share	\$0.35	\$(0.17 )	\$1.06	\$0.88
Dividends declared per share	\$0.24	\$0.22	\$0.72	\$0.66

The accompanying notes are an integral part of these unaudited consolidated financial statements.



Aircastle Limited and Subsidiaries  
 Consolidated Statements of Comprehensive Income (Loss)  
 (Dollars in thousands)  
 (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income (loss)	\$27,437	\$(13,989)	\$83,729	\$71,088
Other comprehensive income, net of tax:				
Net change in fair value of derivatives, net of tax expense of \$0 and \$3 for the three months ended and tax expense of \$0 and \$26 for the nine months ended September 30, 2016 and 2015, respectively	—	272	(1	) 708
Net derivative loss reclassified into earnings	705	5,006	9,074	19,349
Other comprehensive income	705	5,278	9,073	20,057
Total comprehensive income (loss)	\$28,142	\$(8,711	) \$92,802	\$91,145

The accompanying notes are an integral part of these unaudited consolidated financial statements.

Aircastle Limited and Subsidiaries  
Consolidated Statements of Cash Flows  
(Dollars in thousands)  
(Unaudited)

	Nine Months Ended September 30,	
	2016	2015
Cash flows from operating activities:		
Net income	\$83,729	\$71,088
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	227,918	237,538
Amortization of deferred financing costs	13,567	11,211
Amortization of net lease discounts and lease incentives	5,419	10,288
Deferred income taxes	3,129	(1,455 )
Non-cash share-based payment expense	5,796	3,981
Cash flow hedges reclassified into earnings	9,074	19,349
Security deposits and maintenance payments included in earnings	(12,844 )	(20,645 )
Gain on sale of flight equipment	(14,932 )	(43,034 )
Impairment of aircraft	27,185	102,358
Other	(4,712 )	269
Changes in certain assets and liabilities:		
Accounts receivable	1,699	253
Other assets	3,815	(4,382 )
Accounts payable, accrued expenses and other liabilities	16,459	14,085
Lease rentals received in advance	2,111	7,566
Net cash provided by operating activities	367,413	408,470
Cash flows from investing activities:		
Acquisition and improvement of flight equipment	(792,270 )	(1,034,578 )
Proceeds from sale of flight equipment	488,749	343,020
Restricted cash and cash equivalents related to sale of flight equipment	17,000	—
Aircraft purchase deposits and progress payments, net of returned deposits and aircraft sales deposits	(14,035 )	(4,421 )
Net investment in finance and sales-type leases	(78,892 )	(24,000 )
Collections on finance and sales-type leases	14,413	6,768
Unconsolidated equity method investment and associated costs	(12,686 )	—
Other	(812 )	(260 )
Net cash used in investing activities	(378,533 )	(713,471 )
Cash flows from financing activities:		
Repurchase of shares	(36,573 )	(1,960 )
Proceeds from secured and unsecured debt financings	999,350	800,000
Repayments of secured and unsecured debt financings	(489,134 )	(548,359 )
Deferred financing costs	(17,273 )	(12,185 )
Restricted secured liquidity facility collateral	65,000	—
Liquidity facility	(65,000 )	—
Restricted cash and cash equivalents related to financing activities	27,137	14,626
Security deposits and maintenance payments received	123,767	114,644
Security deposits and maintenance payments returned	(37,036 )	(28,797 )
Other	(2,073 )	—
Dividends paid	(56,702 )	(53,583 )
Net cash provided by financing activities	511,463	284,386



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Net increase (decrease) in cash and cash equivalents	500,343	(20,615 )
Cash and cash equivalents at beginning of period	155,904	169,656
Cash and cash equivalents at end of period	\$656,247	\$149,041

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Aircastle Limited and Subsidiaries  
 Consolidated Statements of Cash Flows (Continued)  
 (Dollars in thousands)  
 (Unaudited)

	Nine Months Ended September 30,	
	2016	2015
Supplemental disclosures of cash flow information:		
Cash paid for interest, net of capitalized interest	\$ 141,653	\$ 129,696
Cash paid for income taxes	\$ 12,904	\$ 9,665
Supplemental disclosures of non-cash investing activities:		
Advance lease rentals, security deposits and maintenance payments assumed in asset acquisitions	\$ 110,472	\$ 8,461
Advance lease rentals, security deposits, and maintenance payments settled in sale of flight equipment	\$ 26,671	\$ 77,624
Transfers from Flight equipment held for lease to Net investment in finance and sales-type leases and Other assets	\$ 140,150	\$ 21,766

The accompanying notes are an integral part of these unaudited consolidated financial statements.

Aircastle Limited and Subsidiaries  
Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands, except per share amounts)  
September 30, 2016

Note 1. Summary of Significant Accounting Policies

Organization and Basis of Presentation

Aircastle Limited (“Aircastle,” the “Company,” “we,” “us” or “our”) is a Bermuda exempted company that was incorporated on October 29, 2004 under the provisions of Section 14 of the Companies Act of 1981 of Bermuda. Aircastle’s business is acquiring, leasing, managing and selling commercial jet aircraft.

Aircastle is a holding company that conducts its business through subsidiaries. Aircastle directly or indirectly owns all of the outstanding common shares of its subsidiaries. The consolidated financial statements presented are prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”). The company manages, analyzes and reports on its business and results of operations on the basis of one operating segment: leasing, financing, selling and managing commercial flight equipment. Our chief executive officer is the chief operating decision maker.

The accompanying consolidated financial statements are unaudited and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”) for interim financial reporting and, in our opinion, reflect all adjustments, including normal recurring items, which are necessary to present fairly the results for interim periods. Operating results for the periods presented are not necessarily indicative of the results that may be expected for the entire year. Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with U.S. GAAP have been omitted in accordance with the rules and regulations of the SEC; however, we believe that the disclosures are adequate to make information presented not misleading. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015.

The Company’s management has reviewed and evaluated all events or transactions for potential recognition and/or disclosure since the balance sheet date of September 30, 2016 through the date on which the consolidated financial statements included in this Form 10-Q were issued.

Effective January 1, 2016, the Company adopted Financial Accounting Standards Board (“FASB”) Accounting Standards Update (“ASU”) 2015-02, Consolidation - Amendments to the Consolidation Analysis (Topic 810). The update amended the guidelines for determining whether certain legal entities should be consolidated and reduced the number of consolidation models. This new standard affected reporting entities that are required to evaluate whether they should consolidate certain legal entities. The standard did not have a material impact on our consolidated financial statements and related disclosures.

Principles of Consolidation

The consolidated financial statements include the accounts of Aircastle and all of its subsidiaries. Aircastle consolidates five Variable Interest Entities (“VIEs”) of which Aircastle is the primary beneficiary. All intercompany transactions and balances have been eliminated in consolidation.

We consolidate VIEs in which we have determined that we are the primary beneficiary. We use judgment when deciding: (a) whether an entity is subject to consolidation as a VIE; (b) who the variable interest holders are; (c) the potential expected losses and residual returns of the variable interest holders; and (d) which variable interest holder is the primary beneficiary. When determining which enterprise is the primary beneficiary, we consider: (1) the entity’s purpose and design; (2) which variable interest holder has the power to direct the activities that most significantly impact the entity’s economic performance; and (3) the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the VIE. When certain events occur, we reconsider whether we are the primary beneficiary of VIEs. We do not reconsider whether we are a primary beneficiary solely because of operating losses incurred by an entity.



Aircastle Limited and Subsidiaries  
Notes to Unaudited Consolidated Financial Statements  
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Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. While Aircastle believes that the estimates and related assumptions used in the preparation of the consolidated financial statements are appropriate, actual results could differ from those estimates.

Recent Accounting Pronouncements

On February 25, 2016, the FASB issued Accounting Standards Codification (“ASC”) 842 (“ASC 842”), “Leases,” which replaced the existing guidance in ASC 840, Leases. The accounting for leases by lessors basically remained unchanged from the concepts that existed in ASC 840 accounting. The FASB decided that lessors would be precluded from recognizing selling profit and revenue at lease commencement for any sales-type or direct finance lease that does not transfer control of the underlying asset to the lessee. This requirement aligns the notion of what constitutes a sale in the lessor accounting guidance with that in the forthcoming revenue recognition standard, which evaluates whether a sale has occurred from the customer’s perspective. The standard will be effective for public entities beginning after December 15, 2018. The standard is applied on a “modified retrospective” basis. We plan to adopt the standard on its required effective date of January 1, 2019. We are evaluating the impact that ASC 842 will have on our consolidated financial statements and related disclosures. We do not believe that the adoption of the standard will significantly impact our existing or potential lessees’ economic decisions to lease aircraft.

On May 28, 2014, the FASB and the International Accounting Standards Board (the “IASB”) (collectively, “the Boards”), jointly issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). Lease contracts within the scope of ASC 840, Leases, are specifically excluded from ASU No. 2014-09. The standard’s core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which a company expects to be entitled in exchange for those goods or services. The standard is effective for public entities beginning after December 15, 2017. The standard allows for either “full retrospective” adoption, meaning the standard is applied to all of the periods presented, or “modified retrospective” adoption, meaning the standard is applied only to the most current period presented in the financial statements. We plan to adopt the standard on its required effective date of January 1, 2018. The standard does not impact the accounting of our lease revenue, but may impact the accounting of our revenue other than lease revenue. While we are still performing our analysis, we do not expect the impact of this standard to be material to our consolidated financial statements and related disclosures.

On August 27, 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40). The standard requires management of public companies to evaluate whether there is substantial doubt about the entity’s ability to continue as a going concern and, if so, disclose that fact. Management should evaluate whether there are conditions or events, considered in the aggregate, that raises substantial doubt about the entity’s ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued, when applicable). The standard is effective for annual periods ending after December 15, 2016 and interim periods thereafter, and early adoption is permitted. We do not believe the standard will have a material impact on our consolidated financial statements and related disclosures when adopted.

In March 2016, the FASB issued ASU No. 2016-09, Compensation - Stock Compensation (Topic 718). The update amends the guidelines for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The standard is effective for annual and interim periods beginning January 1, 2017, and early adoption is permitted. We plan to adopt the standard on its required effective date of January 1, 2017. We do not believe the standard will have a material impact on our consolidated financial statements and related disclosures.



Aircastle Limited and Subsidiaries  
Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands, except per share amounts)  
September 30, 2016

Note 2. Fair Value Measurements

Fair value measurements and disclosures require the use of valuation techniques to measure fair value that maximize the use of observable inputs and minimize use of unobservable inputs. These inputs are prioritized as follows:

• Level 1: Observable inputs such as quoted prices in active markets for identical assets or liabilities.

• Level 2: Inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities or market corroborated inputs.

• Level 3: Unobservable inputs for which there is little or no market data and which require us to develop our own assumptions about how market participants price the asset or liability.

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

• The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

• The income approach uses valuation techniques to convert future amounts to a single present amount based on current market expectation about those future amounts.

• The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost).

The following tables set forth our financial assets and liabilities as of September 30, 2016 and December 31, 2015 that we measured at fair value on a recurring basis by level within the fair value hierarchy. 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.

	Fair Value Measurements at September 30, 2016 Using Fair Value Hierarchy				
	Quoted Prices				
	Fair Value as of September 30, 2016	In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Valuation Technique
<b>Assets:</b>					
Cash and cash equivalents	\$ 656,247	\$656,247	\$ —	\$ —	—Market
Restricted cash and cash equivalents	54,000	54,000	—	—	Market
Derivative assets	2,073	—	2,073	—	Market
Total	\$ 712,320	\$ 710,247	\$ 2,073	\$ —	—
<b>Liabilities:</b>					
Derivative liabilities	\$ —	\$ —	\$ —	\$ —	—Income





Aircastle Limited and Subsidiaries  
Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands, except per share amounts)  
September 30, 2016

	Fair Value Measurements at December 31, 2015 Using Fair Value Hierarchy				Valuation Technique
	Fair Value as of December 31, 2015	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
<b>Assets:</b>					
Cash and cash equivalents	\$ 155,904	\$ 155,904	\$ —	\$ —	—Market
Restricted cash and cash equivalents	98,137	98,137	—	—	Market
Derivative assets	—	—	—	—	Market
Total	\$ 254,041	\$ 254,041	\$ —	\$ —	—
<b>Liabilities:</b>					
Derivative liabilities	\$ 1,283	\$ —	\$ 1,283	\$ —	—Income

Our cash and cash equivalents, along with our restricted cash and cash equivalents balances, consist largely of money market securities that are considered to be highly liquid and easily tradable. These securities are valued using inputs observable in active markets for identical securities and are therefore classified as Level 1 within our fair value hierarchy. Our interest rate derivative included in Level 2 consists of United States dollar-denominated interest rate cap, and the fair value is based on market comparisons for similar instruments. We also considered the credit rating and risk of the counterparty providing the interest rate cap based on quantitative and qualitative factors. For the three and nine months ended September 30, 2016 and the year ended December 31, 2015, we had no transfers into or out of Level 3.

We measure the fair value of certain assets and liabilities on a non-recurring basis, when U.S. GAAP requires the application of fair value, including events or changes in circumstances that indicate that the carrying amounts of assets may not be recoverable. Assets subject to these measurements include our investment in an unconsolidated joint venture and aircraft. We account for our investment in an unconsolidated joint venture under the equity method of accounting and record impairment when its fair value is less than its carrying value. We record aircraft at fair value when we determine the carrying value may not be recoverable. Fair value measurements for aircraft in impairment tests are based on an income approach which uses Level 3 inputs, which include the Company's assumptions and appraisal data as to future cash proceeds from leasing and selling aircraft.

#### Aircraft Valuation

##### Recoverability Assessment

We completed our annual recoverability assessment of narrow-body aircraft fleet during the third quarter. We also performed aircraft-specific analyses where there were changes in circumstances, such as approaching lease expirations.

The recoverability assessment is a comparison of the carrying value of each aircraft to its undiscounted expected future cash flows. We develop the assumptions used in the recoverability assessment, including those relating to current and future demand for each aircraft type, based on management's experience in the aircraft leasing industry, as well as information received from third-party sources. Estimates of the undiscounted cash flows for each aircraft type are impacted by changes in contracted and future expected lease rates, residual values, expected scrap values,

economic conditions and other factors.

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Aircastle Limited and Subsidiaries  
Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands, except per share amounts)  
September 30, 2016

In our third quarter 2016 assessment, we reduced economic lives and residuals for all six older Boeing 757-200 aircraft as we intend to sell these aircraft at lease end. As a result, during the three months ended September 30, 2016, we recorded impairment charges totaling \$2,167 relating to two of these aircraft held as operating leases and impairment losses totaling \$2,618 relating to three of these aircraft held as finance leases.

During the second quarter of 2016, we completed our annual recoverability assessment of wide-body and freighter aircraft. As a result of this assessment, we reduced forecasted cash flows for older Airbus A330 aircraft to reflect lower rental expectations given weak demand and increased competition from newer units. As a result, during the three months ended June 30, 2016, we recorded impairment charges totaling \$11,670 and maintenance revenue of \$4,000 relating to one sixteen year old Airbus A330-200 approaching lease expiry.

In our 2015 assessment, we reduced forecasted future cash flows for our six Boeing 747-400 converted freighter aircraft not subject to sales agreements, all of which were more than twenty years old. Our new forecast reflected the persisting glut of supply in the air cargo market resulting from weak growth in demand combined with the growth in capacity arising from new production air freighters and higher belly capacity in latest generation wide-body passenger aircraft. In addition to these market-wide impacts, our older freighters were affected specifically by the imposition of age limits in certain countries and by lower utilization levels.

As a result, we determined that each of our older converted freighter aircraft was on its last lease, and we reduced our residual value assumptions for these aircraft and expected to scrap them following lease expiry. During the third quarter of 2015, we therefore impaired four of these aircraft, which had an aggregate net book value as of August 31, 2015 of \$115,888, writing down their book values by a total of \$34,575, with a fair value date of September 1, 2015. For one of these aircraft, we recorded maintenance revenue of \$5,858, as we no longer planned to reinvest these funds.

#### Other Impairments

During the three months ended September 30, 2016, we reduced forecasted cash flows for three Boeing 747-400 freighter aircraft due to a change in planned engine maintenance events. These three aircraft are nearing the end of their economic lives and leases. As a result, we recorded impairment charges totaling \$5,450, maintenance revenue of \$5,596 and reversed lease incentives of \$2,361.

Also during the three months ended September 30, 2016, we impaired one Airbus A321-200 aircraft for which we had a sales agreement, resulting in an impairment charge of \$1,712. This aircraft was classified as Held for sale in Other assets at September 30, 2016 and sold for its recorded value in October 2016.

During the three months ended June 30, 2016, we entered into an agreement to sell two older Boeing 747-400 freighter aircraft to the lessee resulting in an impairment charge of \$5,053. These two aircraft were classified as Held for sale at June 30, 2016 in Other assets and were subsequently sold in July 2016.

In September 2015, Malaysian Airline System ("MAS") informed us that it was effectively rejecting the lease on our Boeing 777-200ER aircraft as part of its restructuring. This aircraft, which was manufactured in 1998, was the only one of its type in our fleet and the only aircraft we had on lease to MAS. We repossessed it in October 2015. We reduced the carrying value of this aircraft to our best estimate of scrap value. This write-down resulted in an impairment charge of \$37,770, partially offset by \$1,200 of other revenue from a letter of credit we drew following the lease rejection. This aircraft was sold during the second quarter of 2016.

Also in September 2015, we modified the lease agreement with respect to one Airbus A321-200 aircraft. We elected not to reinvest in certain major maintenance events during the lease term, and the lessee agreed to release its rights to certain maintenance payments. As a result, we recorded an impairment charge of \$6,058 and maintenance revenue of \$7,109 for this aircraft.



Aircastle Limited and Subsidiaries  
Notes to Unaudited Consolidated Financial Statements  
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In the second quarter of 2015, we impaired two McDonnell Douglas MD-11 freighter aircraft and one Boeing 737-800 aircraft and recorded impairment charges totaling \$23,955 and maintenance revenue of \$18,234.

Other than the aircraft discussed above, management believes that the net book value of each of our wide-body and freighter aircraft is currently supported by the estimated future undiscounted cash flows expected to be generated by that aircraft, and accordingly, no other aircraft were impaired as a consequence of this recoverability assessment.

However, if our estimates or assumptions change, we may revise our cash flow assumptions and record future impairment charges. While we believe that the estimates and related assumptions used in the recoverability assessment are appropriate, actual results could differ from those estimates.

#### Financial Instruments

Our financial instruments, other than cash, consist principally of cash equivalents, restricted cash and cash equivalents, accounts receivable, accounts payable, amounts borrowed under financings and interest rate derivatives.

The fair value of cash, cash equivalents, restricted cash and cash equivalents, accounts receivable and accounts payable approximates the carrying value of these financial instruments because of their short-term nature.

The fair values of our ECA Financings (as described in Note 6 - Variable Interest Entities below) and Bank Financings are estimated using a discounted cash flow analysis, based on our current incremental borrowing rates for similar types of borrowing arrangements. The fair value of our Senior Notes is estimated using quoted market prices.

The carrying amounts and fair values of our financial instruments at September 30, 2016 and December 31, 2015 are as follows:

	September 30, 2016		December 31, 2015	
	Carrying Amount of Liability	Fair Value of Liability	Carrying Amount of Liability	Fair Value of Liability
Securitizations	\$ —	\$ —	\$125,366	\$123,696
Credit Facilities	120,000	120,000	225,000	225,000
ECA Financings	315,687	333,224	404,491	422,640
Bank Financings	967,519	985,085	636,970	653,699
Senior Notes	3,200,000	3,417,500	2,700,000	2,832,125

All of our financial instruments are classified as Level 2 with the exception of our Senior Notes, which are classified as Level 1.

#### Note 3. Lease Rental Revenues and Flight Equipment Held for Lease

Minimum future annual lease rentals contracted to be received under our existing operating leases of flight equipment at September 30, 2016 were as follows:

Year Ending December 31,	Amount
Remainder of 2016	\$180,010
2017	676,274
2018	613,221
2019	523,645
2020	435,969
Thereafter	1,290,828
Total	\$3,719,947



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Geographic concentration of lease rental revenue earned from flight equipment held for lease was as follows:

Region	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Asia and Pacific	40 %	43 %	40 %	42 %
Europe	22 %	28 %	23 %	28 %
South America	19 %	16 %	19 %	15 %
Middle East and Africa	12 %	9 %	12 %	9 %
North America	7 %	4 %	6 %	6 %
Total	100 %	100 %	100 %	100 %

The classification of regions in the tables above and in the table and discussion below is determined based on the principal location of the lessee of each aircraft.

The following table shows the number of lessees with lease rental revenue of at least 5% and their combined total percentage of lease rental revenue for the years indicated:

	Three Months Ended September 30, 2016		2015		Nine Months Ended September 30, 2016		2015	
	Number of Lessees	Combined % of Lease Rental Revenue	Number of Lessees	Combined % of Lease Rental Revenue	Number of Lessees	Combined % of Lease Rental Revenue	Number of Lessees	Combined % of Lease Rental Revenue
Largest lessees by lease rental revenue	4	25%	2	12%	4	25%	3	17%

The following table sets forth revenue attributable to individual countries representing at least 10% of total revenue (including maintenance revenue) in any year based on each lessee's principal place of business for the years indicated:

Country	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016		2015	
	Revenue	% of Total Revenue	Revenue	% of Total Revenue	Revenue	% of Total Revenue
Indonesia <sup>(1)</sup>	\$21,745	11%	\$61,195	11%	\$—	0%

(1) Total revenue attributable to Indonesia was less than 10% for the three and nine months ended September 30, 2015.





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Geographic concentration of net book value of flight equipment (includes net book value of flight equipment held for lease and net investment in finance and sales-type leases) was as follows:

Region	September 30, 2016			December 31, 2015		
	Number of Aircraft	Net Book Value	%	Number of Aircraft	Net Book Value	%
Asia and Pacific	55	39	%	49	39	%
Europe	57	22	%	64	26	%
South America	23	19	%	22	19	%
Middle East and Africa	14	11	%	9	10	%
North America	24	8	%	17	6	%
Off-lease	2 <sup>(1)</sup>	1	%	1 <sup>(2)</sup>	—	%
Total	175	100	%	162	100	%

(1) Consisted of two Boeing 737-800 aircraft delivered to a customer in China in October 2016.

(2) Consisted of one Boeing 777-200ER aircraft sold during the second quarter of 2016.

The following table sets forth net book value of flight equipment (includes net book value of flight equipment held for lease and net investment in finance and sales-type leases) attributable to individual countries representing at least 10% of net book value of flight equipment based on each lessee's principal place of business as of:

Region	September 30, 2016			December 31, 2015		
	Net Book Value	Net Book Value %	Number of Lessees	Net Book Value	Net Book Value %	Number of Lessees
Indonesia	\$721,704	12%	3	\$661,178	11%	3

At September 30, 2016 and December 31, 2015, the amounts of lease incentive liabilities recorded in maintenance payments on our Consolidated Balance Sheets were \$15,629 and \$21,432, respectively.

#### Note 4. Net Investment in Finance and Sales-Type Leases

At September 30, 2016, our net investment in finance and sales-type leases consisted of fourteen aircraft: eight aircraft leased to two customers in the United States, one aircraft leased to a customer in the Netherlands, three aircraft leased to two customers in Germany, one aircraft leased to a customer in Spain and one aircraft leased to a customer in Sri Lanka. The following table lists the components of our net investment in finance and sales-type leases at September 30, 2016:

	Amount
Total lease payments to be received	\$190,005
Less: Unearned income	(84,096 )
Estimated residual values of leased flight equipment (unguaranteed)	159,945
Net investment in finance and sales-type leases	\$265,854



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At September 30, 2016, minimum future lease payments on finance and sales-type leases are as follows:

Year Ending December 31,	Amount
Remainder of 2016	\$8,844
2017	34,433
2018	27,419
2019	27,249
2020	26,843
Thereafter	65,217
Total lease payments to be received	\$190,005

Note 5. Unconsolidated Equity Method Investment

On December 19, 2013, the Company and an affiliate of Ontario Teachers' Pension Plan ("Teachers'") formed a joint venture ("Lancaster"), in which we hold a 30% equity interest, to invest in leased aircraft. Teachers' holds 10.0% of our outstanding common shares. In March 2016, we sold four Airbus A320-200 aircraft for approximately \$100,000 to Lancaster; these transactions were approved by our Audit Committee as arm's length transactions under our related party policy.

On February 23, 2016, through the Company's relationship with Marubeni Corporation, we established a new joint venture ("IBJ Air") with the leasing arm of the Industrial Bank of Japan, Limited ("IBJL"). IBJ Air is targeted at new narrow-body aircraft leased to premier airlines providing Aircastle with increased access to this market sector and to these customers. During the nine months ended September 30, 2016, we sold two Airbus A320 family aircraft for approximately \$50,000 to IBJ Air, in which we hold a 25% equity interest.

None of these joint ventures qualifies for consolidated accounting treatment. The assets and liabilities of Lancaster and IBJ Air are not included in our Consolidated Balance Sheets and we record our net investment under the equity method of accounting. We source and service investments for Lancaster and IBJ Air and provide marketing, asset management and administrative services to them. We are paid market-based fees for those services, which are recorded in Other revenue in our Consolidated Statements of Income. The Company has recorded in its Consolidated Balance Sheet a \$7,705 guarantee liability in Maintenance payments and a \$5,100 guarantee liability in Security deposits representing its share of the respective exposures.

At September 30, 2016, the net book value of our two joint ventures' eleven aircraft was approximately \$629,000.

	Amount
Investment in joint ventures at December 31, 2015	\$50,377
Investment in joint ventures	13,422
Earnings from joint ventures, net of tax	5,390
Distributions	(2,029 )
Investment in joint ventures at September 30, 2016	\$67,160

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Note 6. Variable Interest Entities

Aircastle consolidates five VIEs of which it is the primary beneficiary. The operating activities of these VIEs are limited to acquiring, owning, leasing, maintaining, operating and, under certain circumstances, selling the seven aircraft discussed below.

Securitization No. 2

In May 2016, we repaid the outstanding amount plus accrued interest and fees due under Securitization No. 2, and ACS Aircraft Finance Ireland 2 Limited became a wholly owned subsidiary of Aircastle.

ECA Financings

Aircastle, through various subsidiaries, each of which is owned by a charitable trust (such entities, collectively the “Air Knight VIEs”), has entered into seven different twelve-year term loans, which are supported by guarantees from Compagnie Française d'Assurance pour le Commerce Extérieur, (“COFACE”), the French government sponsored export credit agency (“ECA”). We refer to these COFACE-supported financings as “ECA Financings.”

Aircastle is the primary beneficiary of the Air Knight VIEs, as we have the power to direct the activities of the VIEs that most significantly impact the economic performance of such VIEs and we bear the significant risk of loss and participate in gains through a finance lease. The activity that most significantly impacts the economic performance is the leasing of aircraft of which our wholly owned subsidiary is the servicer and is responsible for managing the relevant aircraft. There is a cross collateralization guarantee between the Air Knight VIEs. In addition, Aircastle guarantees the debt of the Air Knight VIEs.

The only assets that the Air Knight VIEs have on their books are financing leases that are eliminated in the consolidated financial statements. The related aircraft, with a net book value as of September 30, 2016 of \$521,007, were included in our flight equipment held for lease. The consolidated debt outstanding, net of debt issuance costs, of the Air Knight VIEs as of September 30, 2016 is \$306,103.

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Note 7. Secured and Unsecured Debt Financings

The outstanding amounts of our secured and unsecured term debt financings are as follows:

Debt Obligation	At September 30, 2016			Final Stated Maturity	At
	Outstanding Borrowings	Number of Aircraft	Interest Rate <sup>(1)</sup>		December 31, 2015
Secured Debt Financings:					
Securitization No. 2	\$—	—	—%	—	\$ 125,366
ECA Financings <sup>(2)</sup>	315,687	7	3.02% to 3.96%	12/3/21 to 11/30/24	404,491
Bank Financings <sup>(3)(4)</sup>	967,519	29	1.52% to 5.09%	10/26/17 to 01/19/26	636,970
Less: Debt Issuance Costs	(21,783	) —			(20,589 )
Total secured debt financings, net of debt issuance costs	1,261,423	36			1,146,238
Unsecured Debt Financings:					
Senior Notes due 2017	500,000		6.75%	04/15/17	500,000
Senior Notes due 2018	400,000		4.625%	12/05/18	400,000
Senior Notes due 2019	500,000		6.250%	12/01/19	500,000
Senior Notes due 2020	300,000		7.625%	04/15/20	300,000
Senior Notes due 2021	500,000		5.125%	03/15/21	500,000
Senior Notes due 2022	500,000		5.50%	02/15/22	500,000
Senior Notes due 2023	500,000		5.00%	04/01/23	—
DBJ Term Loan	120,000		2.653%	04/28/19	—
Revolving Credit Facility	—		N/A	05/13/20	225,000
Less: Debt Issuance Costs	(33,696	) —			(30,082 )
Total unsecured debt financings, net of debt issuance costs	3,286,304				2,894,918
Total secured and unsecured debt financings, net of debt issuance costs	\$4,547,727				\$4,041,156

(1) Reflects the floating rate in effect at the applicable reset date plus the margin for our DBJ Term Loan, six of our Bank Financings and our Revolving Credit Facility. All other financings have a fixed rate.

(2) The borrowings under these financings at September 30, 2016 have a weighted-average rate of interest of 3.53%.

(3) The borrowings under these financings at September 30, 2016 have a weighted-average fixed rate of interest of 3.22%.

(4) In September 2016, we purchased an interest rate cap for \$2,283 to hedge approximately 70% of our floating rate interest exposure. The interest rate cap is set at 2% and has a starting notional balance of \$430,000 and reduces

over time to \$215,000. The cap matures in September 2021.

Secured Debt Financings:

Securitization No. 2

On May 9, 2016, we prepaid the outstanding principal balance plus accrued interest and fees due under Securitization No. 2 and terminated the related interest rate derivatives for a total of \$66,262. Upon prepayment of Securitization No. 2, our liquidity facility commitment with HSH Nordbank AG ended and all drawn cash was returned.

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Bank Financings

In June 2016, we entered into a seven-year, full recourse \$434,250 floating rate financing with BNP Paribas, Credit Agricole Corporate and Investment Bank and certain other banks for eighteen aircraft. As of September 30, 2016, we funded sixteen aircraft with an outstanding balance of \$372,784 under this facility. Funding for the final two aircraft was in October 2016 for \$54,900.

Unsecured Debt Financings:

DBJ Term Loan

In March 2016, we entered into a \$120,000 floating rate three-year term loan commitment with Development Bank of Japan Inc. and certain other banks (the "DBJ Term Loan"). This loan was funded in April 2016.

Senior Notes due 2023

On March 21, 2016, Aircastle issued \$500,000 aggregate principal amount of Senior Notes due 2023 (the "Senior Notes due 2023") at par. The Senior Notes due 2023 will mature on April 1, 2023 and bear interest at the rate of 5.00% per annum, payable semi-annually on April 1 and October 1 of each year, commencing on October 1, 2016. Interest accrues on the Senior Notes due 2023 from March 24, 2016.

We may redeem the Senior Notes due 2023 at any time at a redemption price equal to (a) 100% of the principal amount of the notes redeemed, plus accrued and unpaid interest thereon to, but not including, the redemption date and (b) the sum of the present values of the remaining scheduled payments of principal and interest on the notes from the redemption date through the maturity date of the notes (computed using a discount rate equal to the Treasury Rate (as defined in the indenture governing the notes) as of such redemption date plus 50 basis points). In addition, prior to April 1, 2019, we may redeem up to 40% of the aggregate principal amount of the notes issued under the indenture at a redemption price equal to 105% plus accrued and unpaid interest thereon to, but not including, the redemption date, with the net proceeds of certain equity offerings. If the Company undergoes a change of control, it must offer to repurchase the Senior Notes due 2023 at 101% of the principal amount, plus accrued and unpaid interest. The Senior Notes due 2023 are not guaranteed by any of the Company's subsidiaries or any third-party.

Revolving Credit Facility

On March 29, 2016, we increased the size of our unsecured Revolving Credit Facility from \$600,000 to \$675,000 and extended its maturity by one year to May 2020. At September 30, 2016, we had no amounts outstanding under this facility.

As of September 30, 2016, we are in compliance with all applicable covenants in all of our financings.

Note 8. Shareholders' Equity and Share-Based Payment

Performance Stock Units

During the nine months ended September 30, 2016, the Company issued performance share units ("PSUs") to certain employees. These awards were made under the Aircastle Limited 2014 Omnibus Incentive Plan. The PSUs are denominated in share units without dividend rights, each of which is equivalent to one common share, and are subject to performance conditions and time vesting.

The PSUs vest at the end of a three year period which ends on December 31, 2018. Half of the PSUs vest on achieving relative total stockholder return goals (the "TSR PSUs") while the other half vest on attaining annual Adjusted Return on Equity goals (the "AROE PSUs"). The table below shows the PSU awards granted during the nine months ended September 30, 2016, including the number of common shares underlying the awards at the time of grant:

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	Minimum	Target	Maximum
TSR PSUs	—	143,414	286,828
AROE PSUs	—	143,409	286,818
Total	—	286,823	573,646

The fair value of the time based TSR PSUs was determined at the grant date using a Monte Carlo simulation model. Included in the Monte Carlo simulation model were certain assumptions regarding a number of highly complex and subjective variables, such as expected volatility, risk-free interest rate and dividend yield. To appropriately value the award, the risk-free interest rate is estimated for the time period from the valuation date until the vesting date and the historical volatilities were estimated based on a historical time frame equal to the time from the valuation date until the end date of the performance period. The number of TSR PSUs that will ultimately vest is based on the percentile ranking of the Company's TSR among the S&P 400 Index. The number of shares that will ultimately vest will range from 0% to 200% of the target TSR PSUs.

The number of shares vesting from the AROE PSUs at the end of the three-year performance period will depend on the Company's Adjusted Return on Equity as measured against the targets set by the Compensation Committee annually during the performance period, consistent with the business plan approved by the Board. The maximum number of AROE PSUs for 2016 is 95,607. The fair value of the 2016 AROE PSUs was determined based on the closing market price of the Company's common shares on the date of grant reduced by the present value of expected dividends to be paid. The number of shares that will ultimately vest will range from 0% to 200% of the target AROE PSUs.

During the nine months ended September 30, 2016, the Company granted a target of 191,216 PSUs of which 143,414 are TSR PSUs and 47,802 are AROE PSUs. The remaining 95,607 of target AROE PSUs will be considered granted upon the Compensation Committee's setting the target AROE for the respective period. The following table summarizes the activities for our unvested PSUs for the nine months ended September 30, 2016:

	Unvested Performance Stock Units			
	Target Number of Shares of TSR PSUs	Target Number of Shares of AROE PSUs	TSR PSUs Weighted Fair Value at Grant Date Using a Monte Carlo Simulation Model (\$)	AROE PSUs Weighted Fair Value Equal to Adjusted Closing Stock Price on Date of Grant (\$)
Unvested at December 31, 2015	—	—	\$ —	\$ —
Granted	143,414	47,802	25.07	19.18
Unvested as of September 30, 2016	143,414	47,802	\$ 25.07	\$ 19.18
Expected to vest after September 30, 2016	143,414	47,802	\$ 25.07	\$ 19.18



The Company incurred share-based compensation expense related to PSUs of \$852 for the nine months ended September 30, 2016. As of September 30, 2016, there was \$3,660 of unrecognized compensation cost related to unvested stock-based payments granted to certain employees that is expected to be recognized over a weighted-average remaining period of 2.3 years.

During the first nine months of 2016, we acquired 1,827,352 common shares at an aggregate cost of \$34,423, including commissions, under the repurchase program approved by the Company's Board of Directors on February 9, 2016. As of September 30, 2016, the dollar value of common shares remaining under this program is \$96,656. We also repurchased 102,927 shares totaling \$2,150 from our employees and directors to settle tax obligations related to share vesting.

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Note 9. Dividends

The following table sets forth the quarterly dividends declared by our Board of Directors for the periods covered in this report:

Declaration Date	Dividend per Common Share	Aggregate Dividend Amount	Record Date	Payment Date
August 2, 2016	\$ 0.24	\$ 18,872	August 26, 2016	September 15, 2016
May 2, 2016	\$ 0.24	\$ 18,915	May 31, 2016	June 15, 2016
February 9, 2016	\$ 0.24	\$ 18,915	February 29, 2016	March 15, 2016
October 30, 2015	\$ 0.24	\$ 19,377	November 30, 2015	December 15, 2015
August 4, 2015	\$ 0.22	\$ 17,860	August 31, 2015	September 15, 2015

Note 10. Earnings (Loss) Per Share

We include all common shares granted under our incentive compensation plan which remain unvested (“restricted common shares”) and contain non-forfeitable rights to dividends or dividend equivalents, whether paid or unpaid (“participating securities”), in the number of shares outstanding in our basic earnings (loss) per share calculations using the two-class method. All of our restricted common shares are currently participating securities.

Under the two-class method, earnings (loss) per common share is computed by dividing the sum of distributed earnings allocated to common shareholders and undistributed earnings allocated to common shareholders by the weighted-average number of common shares outstanding for the period. In applying the two-class method, distributed and undistributed earnings are allocated to both common shares and restricted common shares based on the total weighted-average shares outstanding during the period. Because the holders of the participating restricted common shares were not contractually required to share in the Company’s losses, in applying the two-class method to compute the basic and diluted net loss per common share, no allocation to restricted common shares was made for the three ended September 30, 2015.

	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016		2015	
Weighted-average shares:						
Common shares outstanding	77,989,933	80,566,400	78,230,011	80,565,754		
Restricted common shares	680,249	645,427	646,299	604,179		
Total weighted-average shares	78,670,182	81,211,827	78,876,310	81,169,933		
Percentage of weighted-average shares:						
Common shares outstanding	99.14	% 99.21	% 99.18	% 99.26	%	
Restricted common shares	0.86	% 0.79	% 0.82	% 0.74	%	
Total percentage of weighted-average shares	100.00	% 100.00	% 100.00	% 100.00	%	



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The calculations of both basic and diluted earnings (loss) per share are as follows:

	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016	
Earnings (loss) per share – Basic:				
Net income (loss)	\$27,437	\$(13,989 )	\$83,729	\$71,088
Less: Distributed and undistributed earnings allocated to restricted common shares <sup>(1)</sup>	(237 )	—	(686 )	(529 )
Earnings (loss) available to common shareholders – Basic	\$27,200	\$(13,989 )	\$83,043	\$70,559
Weighted-average common shares outstanding – Basic	77,989,933	80,566,400	78,230,011	80,565,754
Earnings (loss) per common share – Basic	\$0.35	\$(0.17 )	\$1.06	\$0.88
Earnings (loss) per share – Diluted:				
Net income (loss)	\$27,437	\$(13,989 )	\$83,729	\$71,088
Less: Distributed and undistributed earnings allocated to restricted common shares <sup>(1)</sup>	(237 )	—	(686 )	(529 )
Earnings (loss) available to common shareholders – Diluted	\$27,200	\$(13,989 )	\$83,043	\$70,559
Weighted-average common shares outstanding – Basic	77,989,933	80,566,400	78,230,011	80,565,754
Effect of dilutive shares <sup>(2)</sup>	32,235	—	35,804	—
Weighted-average common shares outstanding – Diluted	78,022,168	80,566,400	78,265,815	80,565,754
Earnings (loss) per common share – Diluted	\$0.35	\$(0.17 )	\$1.06	\$0.88

For the three months ended September 30, 2016, distributed and undistributed earnings to restricted shares are 0.86%, of net income. For the nine months ended September 30, 2016 and 2015, distributed and undistributed earnings to restricted shares are 0.82% and 0.74% of net income, respectively. The amount of restricted share forfeitures for all periods present is immaterial to the allocation of distributed and undistributed earnings.

For the three and nine months ended September 30, 2016, dilutive shares represented contingently issuable shares related to the Company's PSUs. For the three and nine months ended September 30, 2015, we had no dilutive shares.

#### Note 11. Income Taxes

Income taxes have been provided for based upon the tax laws and rates in countries in which our operations are conducted and income is earned. The Company received an assurance from the Bermuda Minister of Finance that it would be exempted from local income, withholding and capital gains taxes until March 2035. Consequently, the provision for income taxes relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily Ireland, Singapore and the United States.

The sources of income (loss) from continuing operations before income taxes and earnings of unconsolidated equity method investment for the three and nine months ended September 30, 2016 and 2015 were as follows:

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	Three Months		Nine Months	
	Ended September		Ended September	
	30,		30,	
	2016	2015	2016	2015
U.S. operations	\$(92 )	\$597	\$1,652	\$1,817
Non-U.S. operations	28,182	(13,434 )	85,469	76,745
Total	\$28,090	\$(12,837)	\$87,121	\$78,562

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All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. The aircraft owning subsidiaries resident in Ireland, Mauritius and Singapore are subject to tax in those respective jurisdictions.

We have a U.S. based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes. We also have Ireland and Singapore based subsidiaries which provide management services to our non-U.S. subsidiaries and are subject to tax in those respective jurisdictions.

The consolidated income tax expense for the three and nine months ended September 30, 2016 and 2015 was determined based upon estimates of the Company's consolidated effective income tax rates for the years ending December 31, 2016 and 2015, respectively.

The Company's effective tax rate for the three and nine months ended September 30, 2016 was 8.8% and 10.1%, respectively, compared to (21.1)% and 15.3% for the three and nine months ended September 30, 2015. Movements in the effective tax rates are generally caused by changes in the proportion of the Company's pre-tax earnings in taxable and non-tax jurisdictions.

Differences between statutory income tax rates and our effective income tax rates applied to pre-tax income consisted of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Notional U.S. federal income tax expense (benefit) at the statutory rate	\$9,831	\$(4,493)	\$30,492	\$27,497
U.S. state and local income tax, net	14	57	139	167
Non-U.S. operations:				
Bermuda	(6,025 )	6,696	(16,687 )	(9,199 )
Ireland	82	2,500	2,155	(407 )
Singapore	(823 )	(1,385 )	(4,874 )	(4,116 )
Other	(752 )	(860 )	(2,835 )	(2,439 )
Non-deductible expenses in the U.S.	133	205	418	566
Other	(2 )	(11 )	(26 )	(32 )
Income tax provision	\$2,458	\$2,709	\$8,782	\$12,037

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Note 12. Interest, Net

The following table shows the components of interest, net:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Interest on borrowings, net settlements on interest rate derivatives, and other liabilities <sup>(1)</sup>	\$57,589	\$51,428	\$166,692	\$153,076
Hedge ineffectiveness losses	—	215	—	509
Amortization of interest rate derivatives related to deferred losses	705	5,006	9,074	19,349
Amortization of deferred financing fees and debt discount <sup>(2)</sup>	4,097	3,746	13,567	11,211
Interest expense	62,391	60,395	189,333	184,145
Less interest income	(546 )	(14 )	(768 )	(82 )
Less capitalized interest	(48 )	—	(75 )	—
Interest, net	\$61,797	\$60,381	\$188,490	\$184,063

(1) For the three and nine months ended September 30, 2016, includes \$0 and \$1,509, respectively, in loan termination fees related to the sale of one aircraft.

(2) For the three and nine months ended September 30, 2016, includes \$0 and \$1,972, respectively, in deferred financing fees written off related to the sale of one aircraft.

Note 13. Commitments and Contingencies

At September 30, 2016, we had commitments to acquire 36 aircraft for \$1,322,989, including 25 Embraer E-2 aircraft. Commitments, including \$140,717 of progress payments, contractual price escalations and other adjustments for these aircraft, at September 30, 2016, net of amounts already paid, are as follows:

Year Ending December 31,	Amount
Remainder of 2016	\$241,761
2017	170,253
2018	258,179
2019	293,756
2020	216,847
Thereafter	142,193
Total	\$1,322,989

Note 14. Other Assets

The following table describes the principal components of other assets on our Consolidated Balance Sheets as of:

	September 30, 2016	December 31, 2015
Deferred federal income tax asset	\$ 1,590	\$ 1,362
Lease incentives and lease premiums, net of amortization of \$36,652 and \$31,623, respectively	78,334	86,874
Flight equipment held for sale <sup>(1)</sup>	17,701	12,901
Other assets	32,215	22,570
Total other assets	\$ 129,840	\$ 123,707

(1) In October 2016, we sold one Airbus A321-200 aircraft.

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Aircastle Limited and Subsidiaries  
Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands, except per share amounts)  
September 30, 2016

Note 15. Accounts Payable, Accrued Expenses and Other Liabilities

The following table describes the principal components of accounts payable, accrued expenses and other liabilities recorded on our Consolidated Balance Sheets as of:

	September 30, 2016	December 31, 2015
Accounts payable and accrued expenses	\$ 23,722	\$ 34,457
Deferred federal income tax liability	38,627	35,269
Accrued interest payable	64,105	37,606
Lease discounts, net of amortization of \$26,544 and \$19,403, respectively	17,686	22,443
Fair value of derivative liabilities	—	1,283
Total accounts payable, accrued expenses and other liabilities	\$ 144,140	\$ 131,058

Note 16. Accumulated Other Comprehensive Loss

The following table describes the principal components of accumulated other comprehensive loss recorded on our Consolidated Balance Sheets:

Changes in accumulated other comprehensive loss by component <sup>(1)</sup>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Beginning balance	\$(4,845)	\$(23,681)	\$(13,213)	\$(38,460)
Amounts recognized in other comprehensive loss on derivatives, net of tax expense of \$0 and \$10 for the three months ended and tax expense of \$0 and \$10 for the nine months ended September 30, 2016 and 2015, respectively	—	(545)	(690)	(1,940)
Amounts reclassified from accumulated other comprehensive loss into income, net of tax expense of \$0 and benefit of \$7 for the three months ended and tax expense of \$0 and \$16 for the nine months ended September 30, 2016 and 2015, respectively	705	5,823	9,763	21,997
Net current period other comprehensive income	705	5,278	9,073	20,057
Ending balance	\$(4,140)	\$(18,403)	\$(4,140)	\$(18,403)

(1) All amounts are net of tax. Amounts in parentheses indicate debits.

Reclassifications from accumulated other comprehensive loss <sup>(1)</sup>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Amount of effective amortization of net deferred interest rate derivative losses <sup>(2)</sup>	\$705	\$5,006	\$9,074	\$19,349
Effective amount of net settlements of interest rate derivatives, net of tax expense of \$0 and benefit of \$7 for the three months ended and tax expense of \$0 and \$16 for the nine months ended September 30, 2016 and 2015, respectively	—	817	689	2,648
Amount of loss reclassified from accumulated other comprehensive loss into income	\$705	\$5,823	\$9,763	\$21,997

(1) All amounts are net of tax.

(2) Included in interest expense.

At September 30, 2016, the amount of deferred net loss expected to be reclassified from OCI into interest expense over the next twelve months related to our terminated interest rate derivatives is \$2,312.

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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This management's discussion and analysis of financial condition and results of operations contains forward-looking statements that involve risks, uncertainties and assumptions. You should read the following discussion in conjunction with our historical consolidated financial statements and the notes thereto appearing elsewhere in this report. The results of operations for the periods reflected herein are not necessarily indicative of results that may be expected for future periods, and our actual results may differ materially from those discussed in the forward-looking statements as a result of various factors, including but not limited to those described under "Risk Factors" and included in our Annual Report on Form 10-K for the year ended December 31, 2015 filed with the Securities and Exchange Commission (the "SEC"). Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States, or U.S. GAAP, and, unless otherwise indicated, the other financial information contained in this report has also been prepared in accordance with U.S. GAAP. Unless otherwise indicated, all references to "dollars" and "\$" in this report are to, and all monetary amounts in this report are presented in, U.S. dollars.

All statements included or incorporated by reference in this Quarterly Report on Form 10-Q (this "report"), other than characterizations of historical fact, are forward-looking statements within the meaning of the federal securities laws, including the Private Securities Litigation Reform Act of 1995. Examples of forward-looking statements include, but are not necessarily limited to, statements relating to our ability to acquire, sell, lease or finance aircraft, raise capital, pay dividends, and increase revenues, earnings, EBITDA, Adjusted EBITDA and Adjusted Net Income and the global aviation industry and aircraft leasing sector. Words such as "anticipates," "expects," "intends," "plans," "projects," "believes," "may," "will," "would," "could," "should," "seeks," "estimates" and variations on these words and similar expressions are intended to identify such forward-looking statements. These statements are based on our historical performance and that of our subsidiaries and on our current plans, estimates and expectations and are subject to a number of factors that could lead to actual results materially different from those described in the forward-looking statements; Aircastle can give no assurance that its expectations will be attained. Accordingly, you should not place undue reliance on any such forward-looking statements which are subject to certain risks and uncertainties that could cause actual results to differ materially from those anticipated as of the date of this report. These risks or uncertainties include, but are not limited to, those described from time to time in Aircastle's filings with the SEC and previously disclosed under "Risk Factors" in Part I - Item 1A of Aircastle's 2015 Annual Report on Form 10-K and elsewhere in this report. In addition, new risks and uncertainties emerge from time to time, and it is not possible for Aircastle to predict or assess the impact of every factor that may cause its actual results to differ from those contained in any forward-looking statements. Such forward-looking statements speak only as of the date of this report. Aircastle expressly disclaims any obligation to revise or update publicly any forward-looking statement to reflect future events or circumstances.

### WEBSITE AND ACCESS TO THE COMPANY'S REPORTS

The Company's Internet website can be found at [www.aircastle.com](http://www.aircastle.com). Our annual reports on Forms 10-K, quarterly reports on Forms 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (the "Exchange Act") are available free of charge through our website under "Investors — SEC Filings" as soon as reasonably practicable after they are electronically filed with, or furnished to, the SEC.

Statements and information concerning our status as a Passive Foreign Investment Company ("PFIC") for U.S. taxpayers are also available free of charge through our website under "Investors — Tax Information (PFIC)." Our Corporate Governance Guidelines, Code of Business Conduct and Ethics, and Board of Directors committee charters (including the charters of the Audit Committee, Compensation Committee, and Nominating and Corporate Governance Committee) are available free of charge through our website under "Investors — Corporate Governance." In addition, our Code of Ethics for the Chief Executive and Senior Financial Officers, which applies to our Chief Executive Officer, Chief Financial Officer, Chief Accounting Officer, Treasurer and Controller, is available in print, free of charge, to any shareholder upon request to Investor Relations, Aircastle Limited, c/o Aircastle Advisor LLC, 300 First Stamford Place, 5th Floor, Stamford, Connecticut 06902.

The information on the Company's Internet website is not part of, or incorporated by reference, into this report, or any other report we file with, or furnish to, the SEC.



## OVERVIEW

Aircastle acquires, leases, and sells commercial jet aircraft to airlines throughout the world. As of September 30, 2016, we owned and managed on behalf of our joint ventures 186 aircraft leased to 65 lessees located in 35 countries. Eleven of these aircraft are managed for our joint ventures with Teachers' and IBJL. Our aircraft are managed by an experienced team based in the United States, Ireland and Singapore. Our aircraft are subject to net leases whereby the lessee is generally responsible for maintaining the aircraft and paying operational, maintenance and insurance costs, although in a majority of cases, we are obligated to pay a portion of specified maintenance or modification costs. As of September 30, 2016, the net book value of our flight equipment and finance lease aircraft was \$6.27 billion compared to \$6.07 billion at December 31, 2015. Our revenues and net income for the three and nine months ended September 30, 2016 were \$194.7 million and \$27.4 million, and \$568.3 million and \$83.7 million, respectively. Growth in commercial air traffic is broadly correlated with world economic activity and in recent years, has been expanding at a rate one and a half to two times that of global GDP growth. The expansion of air travel has driven a rise in the world aircraft fleet. There are currently 19,000 commercial mainline passenger and freighter aircraft in operation worldwide. This fleet is expected to continue expanding at an average annual rate of three to four percent over the next twenty years. In addition, aircraft leasing companies own an increasing share of the world's commercial jet aircraft and now account for approximately 40% of this fleet.

Notwithstanding the sector's long-term growth, the aviation markets have been, and are expected to remain, subject to economic variability, as well as to changes in macroeconomic variables such as fuel price levels and foreign exchange rates. The aviation industry is susceptible to external shocks, such as regional conflicts and terrorist events. Mitigating these risks is the portability of the assets, allowing aircraft to be redeployed to locations where demand is higher.

Air traffic data for the past several years has shown strong passenger market growth. According to the International Air Transport Association, during the first eight months of 2016, global passenger traffic increased 5.8% compared to the same period in 2015. This strong growth was, in part, stimulated by lower air fare prices resulting from the significant drop in fuel prices. Air cargo demand, which is more sensitive to economic conditions, appears to have stabilized. During the first eight months of 2016, air cargo traffic increased 1.4% compared to the same period in 2015, but capacity increased 5.6%, further depressing load factors. This market continues to be hampered by oversupply arising from the rapid growth in belly cargo capacity in passenger aircraft as well as the production of dedicated freighter aircraft.

Demand for air travel varies considerably by region. Emerging market economies have generally been experiencing significant increases in air traffic, driven by rising levels of per capita income. Air traffic growth in some regions is being driven by the proliferation of low cost carriers, which have stimulated demand through lower prices, and by the expansion of long-haul "hub and spoke" traffic, such as that flowing through the Persian Gulf. Mature markets, such as North America and Western Europe, are likely to grow more slowly in tandem with their economies. Airlines operating in areas with political instability or weakening economies, such as those in Russia, Brazil, and now Turkey, are under pressure, and their near-term outlook is more uncertain. On balance, we believe air travel will increase over time, and as a result, we expect demand for modern aircraft will continue to remain strong over the long-term.

Low fuel prices and record low interest rates are having substantial effects on our industry. With jet fuel at less than half its cost compared to three years ago, airlines have been able to reduce ticket prices and stimulate aircraft traffic while retaining enough of this benefit to achieve record profit levels. We believe the prospect of fuel prices remaining low for some time is shifting lease pricing among different types of aircraft, generally to the detriment of newer, more fuel efficient aircraft with higher capital costs. At the same time, low interest rates and strong overall industry performance is drawing significant capital to our business and increasing competition for new investments.

Capital availability for aircraft has varied over time, and we consider this variability to be a basic characteristic of our business. If pursued properly, this represents an important source of opportunity. Both debt and equity markets have improved globally over the past several years with the recovery from the global financial crisis. Strong U.S. debt capital market conditions benefited borrowers by permitting access to financing at historic lows while higher fees have driven down export credit agency ("ECA") demand. Recently, ECA availability has been curtailed, both in the U.S. and in Europe, due to political issues and an investigation into possible irregularities, respectively. Commercial bank debt continues to play a critical role for aircraft finance, although we believe regulatory pressures will ultimately limit its role.

While financial markets conditions are currently attractive, heightened volatility stemming from global growth concerns and various geopolitical issues may increase capital costs and limit availability going forward. We believe these market

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forces should generate attractive new investment and trading opportunities upon which we are well placed to capitalize given our access to different financing sources, our limited capital commitments and our reputation as a reliable trading partner. Over the longer term, our strategy is to achieve an investment grade credit rating, which we believe will reduce our borrowing costs and enable more reliable access to debt capital throughout the business cycle. We believe our business approach is differentiated from those of other large leasing companies. Our investment strategy is to seek out the best risk-adjusted return opportunities across the commercial jet market, so our acquisition targets and growth rates vary with market conditions. We prefer to have capital resources available to capture investment opportunities that arise in the context of changing market circumstances. As such, we limit large, long-term capital commitments and are therefore much less reliant on orders for new aircraft from aircraft manufacturers as a source of new investments. In general, we focus on discerning investment value in situations that are often more bespoke and generally less competitive.

We plan to grow our business and profits over the long-term while maintaining a countercyclical orientation, a bias towards limiting long-dated capital commitments and a conservative and flexible capital structure. Our business strategy entails the following elements:

**Pursuing a disciplined and differentiated investment strategy.** In our view, aircraft values change in different ways over time. As a consequence, we carefully evaluate investments across different aircraft models, ages, lessees and acquisition sources and re-evaluate these choices periodically as market conditions and relative investment values change. We believe the financing flexibility offered through unsecured debt and our team's experience with a wide range of asset types enables our value oriented strategy and provides us with a competitive advantage for many investment opportunities. We view orders from equipment manufacturers to be part of our investment opportunity set but choose to limit long term capital commitments unless we believe there is an adequate return premium to compensate for risks and opportunity costs.

**Originating investments from many different sources across the globe.** Our strategy is to seek out worthwhile investments broadly leveraging our team's wide range of contacts around the world. We utilize a multi-channel approach to sourcing acquisitions and have purchased aircraft from a large number of airlines, lessors, original equipment manufacturers, lenders and other aircraft owners. Since our formation in 2004, we have acquired aircraft from 80 different sellers.

**Maintaining a conservative capital commitment profile.** We choose to limit long-term capital commitments unless we believe there to be an adequate return premium to compensate for the related risks and opportunity costs. This approach sets us apart from most other large aircraft leasing companies.

**Leveraging our strategic relationships.** We intend to capture the benefits provided through the extensive global contacts and relationships maintained by Marubeni Corporation, which is our biggest shareholder and one of the largest Japanese trading companies. Marubeni has already enabled greater access to Japanese-based financing and helped source and develop our new joint venture with IBJ Leasing. Our joint venture with Teachers' provides us with an opportunity to pursue larger transactions, manage portfolio concentrations and improve our return on deployed capital.

**Maintaining efficient access to capital from a wide set of sources while targeting an investment grade credit rating.**

We believe the aircraft investment market is subject to forces related to the business cycle and our strategy is to increase our purchase activity when prices are low and to emphasize asset sales when competition for assets is high. To implement this approach, we believe it is very important to maintain access to a wide variety of financing sources. Our strategy is to improve our corporate credit ratings to an investment grade level by maintaining strong portfolio and capital structure metrics while achieving a critical size through accretive growth. We believe improving our credit rating will not only reduce our borrowing costs but also facilitate more reliable access to both secured and unsecured debt capital throughout the business cycle.

**Selling assets when attractive opportunities arise and for portfolio management purposes.** We pursue asset sales, as opportunities arise over the course of the business cycle, with the aim of realizing profits and reinvesting proceeds where more accretive investments are available. We also use asset sales for portfolio management purposes, such as reducing lessee specific concentrations and lowering residual value exposures to certain aircraft types, and as an exit from investments when a sale would provide the greatest expected cash flow for us.

Capturing the value of our efficient operating platform and strong operating track record. We believe our team's capabilities in the global aircraft leasing market place us in a favorable position to source and manage new income-generating activities. We intend to continue to focus our efforts in areas where we believe we have competitive advantages, including new direct investments as well as ventures with strategic business partners.



Intending to pay quarterly dividends to our shareholders based on the Company's sustainable earnings levels. Aircastle has paid dividends each quarter since our initial public offering in 2006. On August 2, 2016, our Board of Directors declared a regular quarterly dividend of \$0.24 per common share, or an aggregate of \$18.9 million for the three months ended September 30, 2016, which was paid on September 15, 2016 to holders of record on August 26, 2016. These dividends may not be indicative of the amount of any future dividends. Our ability to pay quarterly dividends will depend upon many factors, including those as described in Item 1A. "Risk Factors" and elsewhere in our 2015 Annual Report on Form 10-K.

#### Revenues

Our revenues are comprised primarily of operating lease rentals on flight equipment held for lease, revenue from retained maintenance payments related to lease expirations, lease termination payments, lease incentive amortization and interest recognized from finance and sales-type leases.

Typically, our aircraft are subject to net leases whereby the lessee pays lease rentals and is generally responsible for maintaining the aircraft and paying operational, maintenance and insurance costs arising during the term of the lease. Our aircraft lease agreements generally provide for the periodic payment of a fixed amount of rent over the life of the lease and the amount of the contracted rent will depend upon the type, age, specification and condition of the aircraft and market conditions at the time the lease is committed. The amount of rent we receive will depend on a number of factors, including the creditworthiness of our lessees and the occurrence of restructurings and defaults. Our lease rental revenues are also affected by the extent to which aircraft are off-lease and our ability to remarket aircraft that are nearing the end of their leases in order to minimize their off-lease time. Our success in re-leasing aircraft is affected by market conditions relating to our aircraft and by general industry conditions and trends. An increase in the percentage of off-lease aircraft or a reduction in lease rates upon remarketing would negatively impact our revenues. Under an operating lease, the lessee will be responsible for performing maintenance on the relevant aircraft and will typically be required to make payments to us for heavy maintenance, overhaul or replacement of certain high-value components of the aircraft. These maintenance payments are based on hours or cycles of utilization or on calendar time, depending upon the component, and would be made either monthly in arrears or at the end of the lease term. For maintenance payments made monthly in arrears during a lease term, we will typically be required to reimburse all or a portion of these payments to the lessee upon their completion of the relevant heavy maintenance, overhaul or parts replacement. We record maintenance payments paid by the lessee during a lease as accrued maintenance liabilities in recognition of our obligation in the lease to refund such payments, and therefore we do not recognize maintenance revenue during the lease. Maintenance revenue recognition would occur at the end of a lease, when we are able to determine the amount, if any, by which reserve payments received exceed the amount we are required under the lease to reimburse to the lessee for heavy maintenance, overhaul or parts replacement. The amount of maintenance revenue we recognize in any reporting period is inherently volatile and is dependent upon a number of factors, including the timing of lease expiries, including scheduled and unscheduled expiries, the timing of maintenance events and the utilization of the aircraft by the lessee.

Many of our leases contain provisions which may require us to pay a portion of the lessee's costs for heavy maintenance, overhaul or replacement of certain high-value components. We account for these expected payments as lease incentives, which are amortized as a reduction of revenue over the life of the lease. We estimate the amount of our portion for such costs, typically for the first major maintenance event for the airframe, engines, landing gear and auxiliary power units, expected to be paid to the lessee based on assumed utilization of the related aircraft by the lessee, the anticipated cost of the maintenance event and the estimated amounts the lessee is responsible to pay. This estimated lease incentive is not recognized as a lease incentive liability at the inception of the lease. We recognize the lease incentive as a reduction of lease revenue on a straight-line basis over the life of the lease, with the offset being recorded as a lease incentive liability which is included in maintenance payments on the balance sheet. The payment to the lessee for the lease incentive liability is first recorded against the lease incentive liability and any excess above the lease incentive liability is recorded as a prepaid lease incentive asset which is included in other assets on the balance sheet and continues to amortize over the remaining life of the lease.

#### 2016 Lease Expirations and Lease Placements

At September 30, 2016, we had two aircraft scheduled to come off lease during 2016 for which we have not yet secured a lease or sales commitments. We have since secured a lease commitment for one of these aircraft and a sale

commitment for the other.

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#### 2017-2020 Lease Expirations and Lease Placements

Taking into account lease and sale commitments, we currently have the following number of aircraft with lease expirations scheduled in the period 2017-2020, representing the percentage of our net book value of flight equipment (including flight equipment held for lease and net investment in finance and sales-type leases) at September 30, 2016, specified below:

2017: 16 aircraft, representing 8%;

2018: 15 aircraft, representing 11%;

2019: 17 aircraft, representing 11%; and

2020: 24 aircraft, representing 8%.

#### Operating Expenses

Operating expenses are comprised of depreciation of flight equipment held for lease, interest expense, selling, general and administrative expenses, aircraft impairment charges and maintenance and other costs. Because our operating lease terms generally require the lessee to pay for operating, maintenance and insurance costs, our portion of maintenance and other costs relating to aircraft reflected in our statement of income primarily relates to expenses for unscheduled lease terminations.

#### Income Tax Provision

We obtained an assurance from the Minister of Finance of Bermuda under the Exempted Undertakings Tax Protection Act 1966 that, in the event any legislation is enacted in Bermuda imposing any tax computed on profits or income, or computed on any capital asset, gain or appreciation or any tax in the nature of estate duty or inheritance tax, such tax shall not, until March 2035, be applicable to us or to any of our operations or to our shares, debentures or other obligations except insofar as such tax applies to persons ordinarily resident in Bermuda or to any taxes payable by us in respect of real property owned or leased by us in Bermuda. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily Ireland, Singapore and the United States.

All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes, unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. The aircraft owning subsidiaries resident in Ireland, Mauritius and Singapore are subject to tax in those respective jurisdictions.

We have a U.S.-based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes. We also have Ireland and Singapore based subsidiaries which provide management services to our non-U.S. subsidiaries and are subject to tax in those respective jurisdictions.

#### Acquisitions and Sales

During the first nine months of 2016, we acquired 32 aircraft for \$961.1 million. At September 30, 2016, we had commitments to acquire 36 additional aircraft for \$1.32 billion, including the acquisition of 25 new E-Jet E-2 aircraft from Embraer, which are scheduled to deliver in 2018 to 2021. As of October 28, 2016, we have commitments to acquire 37 aircraft for \$1.36 billion.

During the first nine months of 2016, we sold nineteen aircraft and other flight equipment for \$488.7 million, which resulted in a net gain of \$14.9 million.

The following table sets forth certain information with respect to the aircraft owned by us as of September 30, 2016:  
AIRCATTLE AIRCRAFT INFORMATION (dollars in millions)

	As of September 30, 2016 <sup>(1)</sup>	As of September 30, 2015 <sup>(1)</sup>		
Owned Aircraft				
Flight Equipment	\$ 6,270	\$ 6,007		
Unencumbered Flight Equipment <sup>(2)</sup>	\$ 4,343	\$ 3,722		
Number of Aircraft	175	160		
Number of Unencumbered Aircraft <sup>(2)</sup>	139	109		
Number of Lessees	65	51		
Number of Countries	35	32		
Weighted Average Age (years) <sup>(3)</sup>	7.6	7.7		
Weighted Average Remaining Lease Term (years) <sup>(3)</sup>	5.3	5.9		
Weighted Average Fleet Utilization during the three months ended September 30, 2016 and 2015 <sup>(4)</sup>	98.2	% 99.9	%	
Weighted Average Fleet Utilization during the nine months ended September 30, 2016 and 2015 <sup>(4)</sup>	98.9	% 99.2	%	
Portfolio Yield for the three months ended September 30, 2016 and 2015 <sup>(5)</sup>	12.4	% 12.7	%	
Portfolio Yield for the nine months ended September 30, 2016 and 2015 <sup>(5)</sup>	12.4	% 12.7	%	
Managed Aircraft				
Flight Equipment	\$ 629	\$ 489		
Number of Aircraft	11	5		

(1) Calculated using net book value of flight equipment held for lease and net investment in finance and sales-type leases at period end.

(2) At September 30, 2016, includes two aircraft with a net book value of \$76.3 million that secure our ACS 2016 Bank Financing.

(3) Weighted by net book value.

(4) Aircraft on-lease days as a percent of total days in period weighted by net book value.

Lease rental revenue, interest income and cash collections on our net investment in finance and sales-type leases for the period as a percent of the average net book value of flight equipment held for lease and net investment in finance and sales-type leases for the period; quarterly information is annualized. Based on the growing level of finance and sales-type lease revenue, management revised the calculation of portfolio yield to include our net investment in finance and sales-type leases in the average net book value and to include the interest income and cash collections on our net investment in finance and sales-type leases in lease rentals.

Our owned aircraft portfolio as of September 30, 2016 is listed in Exhibit 99.1 to this report.

## PORTFOLIO DIVERSIFICATION

Aircraft Type	Owned Aircraft as of September 30, 2016			Owned Aircraft as of September 30, 2015		
	Number of Aircraft	% of Net Book Value <sup>(1)</sup>	%	Number of Aircraft	% of Net Book Value <sup>(1)</sup>	%
<b>Passenger:</b>						
Narrow-body	134	52	%	113	44	%
Wide-body	32	40	%	34	44	%
Total Passenger	166	92	%	147	88	%
Freighter	9	8	%	13	12	%
Total	175	100	%	160	100	%
<b>Manufacturer</b>						
Airbus	87	50	%	85	53	%
Boeing	83	48	%	70	45	%
Embraer	5	2	%	5	2	%
Total	175	100	%	160	100	%
<b>Regional Diversification</b>						
Asia and Pacific	55	39	%	54	42	%
Europe	57	22	%	66	27	%
South America	23	19	%	18	17	%
Middle East and Africa	14	11	%	6	9	%
North America	24	8	%	15	5	%
Off-lease	2	<sup>(2)</sup> 1	%	1	<sup>(3)</sup> —	%
Total	175	100	%	160	100	%

(1) Calculated using net book value of flight equipment held for lease and net investment in finance and sales-type leases at period end.

(2) Consisted of two Boeing 737-800 aircraft delivered to a customer in China in October 2016.

(3) Consisted of one Boeing 777-200ER aircraft sold in the second quarter of 2016.

Our largest customer represents 7.2% of the net book value of flight equipment held for lease (includes net book value of flight equipment held for lease and net investment in finance and sales-type leases) at September 30, 2016. Our top fifteen customers for aircraft we owned at September 30, 2016, representing 82 aircraft and 63% of the net book value of flight equipment held for lease, are as follows:

Percent of Net Book Value	Customer	Country	Number of Aircraft
Greater than 6% per customer	Lion Air	Indonesia	13
	Avianca Brazil	Brazil	10
3% to 6% per customer	LATAM	Chile	3
	South African Airways	South Africa	4
	Thai Airways	Thailand	2
	Singapore Airlines	Singapore	4
	AirAsia X	Malaysia	3
	Air Berlin	Germany	11
	Emirates	United Arab Emirates	2
	AirBridgeCargo <sup>(1)</sup>	Russia	2
	Jet Airways	India	8
	Iberia	Spain	11
	Garuda	Indonesia	4
Less than 3% per customer	Avianca	Colombia	2
	Air Canada	Canada	3

(1) Guaranteed by Volga-Dnepr Airlines. When combined with an affiliated airline, this exposure represents 4% of net book value of flight equipment held for lease and net investment in finance and sales-type leases at period end.

#### Finance

We intend to fund new investments through cash on hand, funds generated from operations, maintenance payments received from lessees, secured borrowings for aircraft, draws on our Revolving Credit Facility and proceeds from any future aircraft sales. We may repay all or a portion of such borrowings from time to time with the net proceeds from subsequent long-term debt financings, additional equity offerings or cash generated from operations and asset sales. Therefore, our ability to execute our business strategy, particularly the acquisition of additional commercial jet aircraft or other aviation assets, depends to a significant degree on our ability to obtain additional debt and equity capital on terms we deem attractive.

See “Liquidity and Capital Resources” below.

## RESULTS OF OPERATIONS

Comparison of the three months ended September 30, 2016 to the three months ended September 30, 2015:

	Three Months Ended September 30, 2016      2015 (Dollars in thousands)	
Revenues:		
Lease rental revenue	\$181,975	\$188,038
Finance and sales-type lease revenue	5,354	1,868
Amortization of net lease discounts and lease incentives	(521 )	(2,113 )
Maintenance revenue	6,829	15,726
Total lease revenue	193,637	203,519
Other revenue	1,015	8,555
Total revenues	194,652	212,074
Operating expenses:		
Depreciation	76,201	85,324
Interest, net	61,797	60,381
Selling, general and administrative	15,985	14,032
Impairment of aircraft	10,462	78,403
Maintenance and other costs	1,834	2,520
Total operating expenses	166,279	240,660
Other income (expense):		
Gain (loss) on sale of flight equipment	(73 )	15,679
Other	(210 )	70
Total other income (expense)	(283 )	15,749
Income (loss) from continuing operations before income taxes and earnings of unconsolidated equity method investment	28,090	(12,837 )
Income tax provision	2,458	2,709
Earnings of unconsolidated equity method investment, net of tax	1,805	1,557
Net income (loss)	\$27,437	\$(13,989 )

## Revenues

Total revenues decreased by 8.2%, or \$17.4 million, for the three months ended September 30, 2016 as compared to the three months ended September 30, 2015.

Lease rental revenue. The decrease in lease rental revenue of \$6.1 million for the three months ended September 30, 2016, as compared to the same period in 2015, was primarily the result of decreases in revenue of:

\$26.4 million due to sales of 35 aircraft since September 30, 2015; and

\$8.5 million due to lease extensions, amendments, transitions and other changes.

These decreases were partially offset by a \$28.8 million increase in revenue reflecting the impact of 28 aircraft purchased in 2016 and sixteen aircraft purchased in 2015.

Finance and sales-type lease revenue. For the three months ended September 30, 2016, \$5.4 million of interest income from finance and sales-type leases was recognized, as compared to \$1.9 million of interest income from finance and sales-type leases recorded for the same period in 2015, due to the addition of seven aircraft over the last twelve months, partially offset by the sale of one aircraft over the last twelve months.

Amortization of net lease discounts and lease incentives consisted of the following:

	Three Months Ended September 30, 2016 2015 (Dollars in thousands)	
Amortization of lease incentives	\$42	\$(1,846)
Amortization of lease premiums	(2,894)	(2,852)
Amortization of lease discounts	2,331	2,585
Amortization of net lease discounts and lease incentives	\$(521)	\$(2,113)

As more fully described above under “Revenues,” lease incentives represent our estimated portion of the lessee’s cost for heavy maintenance, overhaul or replacement of certain high-value components, which are amortized over the life of the related lease. As we enter into new leases, the amortization of lease incentives generally increases and, conversely, if a related lease terminates, the related unused lease incentive liability will reduce the amortization of lease incentives. The decrease in amortization of lease incentives of \$1.9 million for the three months ended September 30, 2016, as compared to the same period in 2015, was primarily attributable to the sale of six aircraft and changes in estimate related to engines for three freighter aircraft of \$3.7 million, partially offset by a \$2.6 million reversal related to the transition of one aircraft.

**Maintenance revenue.** For the three months ended September 30, 2016, we recorded \$6.8 million of maintenance revenue, including \$5.6 million related to maintenance reserves taken into income for three freighter aircraft. For the same period in 2015, we recorded \$15.7 million of maintenance revenue from four scheduled lease terminations.

**Other revenue.** For the three months ended September 30, 2016, we recorded \$1.0 million of other revenue. For the same period in 2015, we recorded \$8.6 million of other revenue, primarily from fees earned from three lessees in connection with the early termination of four leases.

**Operating expenses**

Total operating expenses decreased by 30.9%, or \$74.4 million, for the three months ended September 30, 2016, as compared to the three months ended September 30, 2015.

Depreciation expense decreased by 10.7%, or \$9.1 million, for the three months ended September 30, 2016 as compared to the same period in 2015. The decrease is primarily the result of lower depreciation of:

\$18.3 million due to aircraft sales; and

\$2.5 million due to changes in asset lives, residual values and other changes.

This decrease was partially offset by an \$11.7 million increase due to aircraft acquired.

Interest, net consisted of the following:

	Three Months Ended September 30, 2016 2015 (Dollars in thousands)	
Interest on borrowings, net of settlements on interest rate derivatives, and other liabilities	\$57,589	\$51,428
Hedge ineffectiveness losses	—	215
Amortization of interest rate derivatives related to deferred losses	705	5,006
Amortization of deferred financing fees and debt discount	4,097	3,746
Interest expense	62,391	60,395
Less: interest income	(546)	(14)
Less: capitalized interest	(48)	—
Interest, net	\$61,797	\$60,381





Interest, net increased by \$1.4 million, or 2.3%, over the three months ended September 30, 2015. The net increase is the result of higher interest on borrowings of \$6.2 million, driven by higher weighted-average debt outstanding as compared to a year ago. This increase was partially offset by a \$4.3 million decrease in amortization of interest rate derivatives related to deferred losses.

Selling, general and administrative expenses for the three months ended September 30, 2016 increased by \$2.0 million over the same period in 2015, as a result of higher personnel and rent costs. Non-cash share-based expense was \$2.1 million and \$1.4 million for the three months ended September 30, 2016 and 2015, respectively.

Impairment of Aircraft. See “Summary of Impairments and Recoverability Assessment” below for a detailed discussion of impairment charges related to certain aircraft.

Maintenance and other costs were \$1.8 million for the three months ended September 30, 2016, essentially flat compared to the same period in 2015.

Other income (expense)

Gain (loss) on sale of flight equipment decreased by \$15.8 million, to a \$0.1 million loss for the three months ended September 30, 2016, compared with a gain of \$15.7 million for the same period in 2015. During the third quarter of 2016, we recorded gains totaling \$7.8 million and losses totaling \$7.9 million, primarily due to a loss of \$5.2 million for an Airbus A-330-200 aircraft’s lease extension classified as a sales type lease. During the third quarter of 2015, all aircraft sold were for gains or at recorded value.

Income tax provision

Our provision for income taxes for the three months ended September 30, 2016 and 2015 was \$2.5 million and \$2.7 million, respectively. Income taxes have been provided based on the applicable tax laws and rates of those countries in which operations are conducted and income is earned, primarily Ireland, Singapore and the United States. The decrease in our income tax provision of approximately \$0.3 million for the three months ended September 30, 2016, as compared to the same period in 2015, was primarily attributable to changes in operating income subject to tax in Ireland, Singapore, the United States and other jurisdictions.

All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. The aircraft owning subsidiaries resident in Ireland, Mauritius and Singapore are subject to tax in those respective jurisdictions.

We have a U.S.-based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes. In addition, we have Ireland and Singapore based subsidiaries which provide management services to our non-U.S. subsidiaries and are subject to tax in those respective jurisdictions.

The Company received an assurance from the Bermuda Minister of Finance that it would be exempted from local income, withholding and capital gains taxes until March 2035. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily the United States and Ireland.

Other comprehensive income (loss)

Other comprehensive income consisted of the following:

	Three Months Ended September 30,	
	2016	2015
	(Dollars in thousands)	
Net income (loss)	\$27,437	\$(13,989)
Net change in fair value of derivatives, net of tax benefit of \$0 and \$3, respectively	—	272
Derivative loss reclassified into earnings	705	5,006
Total comprehensive income (loss)	\$28,142	\$(8,711 )



Other comprehensive income (loss) increased by \$36.9 million for the three months ended September 30, 2016, as a result of a \$41.4 million increase in net income and a decrease of \$4.3 million in amortization of deferred net losses reclassified into earnings related to terminated interest rate derivatives compared to the same period in 2015.

## RESULTS OF OPERATIONS

Comparison of the nine months ended September 30, 2016 to the nine months ended September 30, 2015:

	Nine Months Ended September 30, 2016      2015 (Dollars in thousands)	
Revenues:		
Lease rental revenue	\$537,670	\$550,023
Finance and sales-type lease revenue	13,026	5,352
Amortization of net lease discounts and lease incentives	(5,419 )	(10,288 )
Maintenance revenue	20,603	55,148
Total lease revenue	565,880	600,235
Other revenue	2,425	10,700
Total revenues	568,305	610,935
Operating expenses:		
Depreciation	227,918	237,538
Interest, net	188,490	184,063
Selling, general and administrative	46,883	42,663
Impairment of aircraft	27,185	102,358
Maintenance and other costs	5,504	9,126
Total operating expenses	495,980	575,748
Other income (expense):		
Gain on sale of flight equipment	14,932	43,034
Other	(136 )	341
Total other income	14,796	43,375
Income from continuing operations before income taxes and earnings of unconsolidated equity method investment	87,121	78,562
Income tax provision	8,782	12,037
Earnings of unconsolidated equity method investment, net of tax	5,390	4,563
Net income	\$83,729	\$71,088

## Revenues

Total revenues decreased by 7.0%, or \$42.6 million, for the nine months ended September 30, 2016 as compared to the nine months ended September 30, 2015.

Lease rental revenue. The decrease in lease rental revenue of \$12.4 million for the nine months ended September 30, 2016 as compared to the same period in 2015 was primarily the result of decreases in revenue of:

\$80.4 million due to sales of 45 aircraft since September 30, 2015; and

\$15.7 million due to lease extensions, amendments, transitions and other changes.

These decreases were partially offset by an \$83.8 million increase in revenue reflecting the 28 aircraft purchased in 2016 and 35 aircraft purchased in 2015.

Finance and sales-type lease revenue. For the nine months ended September 30, 2016, \$13.0 million of interest income from finance and sales-type leases was recognized as compared to \$5.4 million of interest income from finance and sales-type leases recorded for the same period in 2015 due to the addition of seven aircraft over the last twelve months, partially offset by the sale of one aircraft over the last twelve months.

Amortization of net lease premiums, discounts and lease incentives.

	Nine Months Ended September 30, 2016	
	2016	2015
	(Dollars in thousands)	
Amortization of lease incentives	\$(3,989)	\$(9,597 )
Amortization of lease premiums	(8,571 )	(8,218 )
Amortization of lease discounts	7,141	7,527
Amortization of net lease premiums, discounts and lease incentives	\$(5,419)	\$(10,288)

As more fully described above under "Revenues," lease incentives represent our estimated portion of the lessee's cost for heavy maintenance, overhaul or replacement of certain high-value components which is amortized over the life of the related lease. As we enter into new leases, the amortization of lease incentives generally increases and, conversely, if a related lease terminates, the related unused lease incentive liability will reduce the amortization of lease incentives. The decrease in amortization of lease incentives of \$5.6 million for the nine months ended September 30, 2016 as compared to the same period in 2015 was primarily attributable to the sale of ten aircraft and changes in estimate related to engines for three freighter aircraft of \$8.2 million, partially offset by \$3.6 million in reversals related to the transition of six aircraft.

**Maintenance revenue.** For the nine months ended September 30, 2016, we recorded \$20.6 million of maintenance revenue from one scheduled lease termination for \$6.9 million and maintenance reserves taken into income for three freighter aircraft and one wide-body aircraft totaling \$13.2 million. For the same period in 2015, we recorded \$55.1 million of maintenance revenue from fifteen scheduled lease terminations.

**Other revenue.** For the nine months ended September 30, 2016, we recorded \$2.4 million of other revenue. For the same period in 2015, we recorded \$10.7 million of other revenue, primarily from fees earned from five lessees in connection with the early termination of ten leases.

#### Operating expenses

Total operating expenses decreased by 13.9%, or \$79.8 million, for the nine months ended September 30, 2016 as compared to the nine months ended September 30, 2015.

Depreciation expense decreased by 4.0%, or \$9.6 million, for the nine months ended September 30, 2016 as compared to the same period in 2015. The net decrease is primarily the result of lower depreciation of \$50.9 million due to aircraft sales.

This decrease was partially offset by:

- \$34.9 million increase due to aircraft acquired; and
- \$6.3 million increase due to changes in asset lives, residual values and other changes.

Interest, net consisted of the following:

	Nine Months Ended September 30,	
	2016	2015
	(Dollars in thousands)	
Interest on borrowings, net of settlements on interest rate derivatives, and other liabilities <sup>(1)</sup>	\$166,692	\$153,076
Hedge ineffectiveness losses	—	509
Amortization of interest rate derivatives related to deferred losses	9,074	19,349
Amortization of deferred financing fees and debt discount <sup>(2)</sup>	13,567	11,211
Interest expense	189,333	184,145
Less: interest income	(768 )	(82 )
Less: capitalized interest	(75 )	—
Interest, net	\$188,490	\$184,063

(1) For the nine months ended September 30, 2016, includes \$1,509 in loan termination fees related to the sale of one aircraft.

(2) For the nine months ended September 30, 2016, includes \$1,972 in deferred financing fees written off related to the sale of one aircraft.

Interest, net increased by \$4.4 million, or 2.4%, over the nine months ended September 30, 2015. The net increase is primarily a result of higher interest on borrowings of \$13.6 million, driven by an increase of \$12.1 million from higher weighted average debt outstanding and a \$1.5 million loan termination fee related to the sale of an aircraft during the nine months ended September 30, 2016 as compared to a year ago. These increases were partially offset by a \$10.3 million decrease in amortization of interest rate derivatives related to deferred losses.

Selling, general and administrative expenses for the nine months ended September 30, 2016 increased \$4.2 million over the same period in 2015 as a result of higher personnel and rent costs. Non-cash share-based expense was \$5.8 million and \$4.0 million for the nine months ended September 30, 2016 and 2015, respectively.

Impairment of Aircraft. See “Summary of Impairments and Recoverability Assessment” below for a detailed discussion of impairment charges related to certain aircraft.

Maintenance and other costs were \$5.5 million for the nine months ended September 30, 2016, a decrease of \$3.6 million over the same period in 2015. The net decrease is primarily related to lower maintenance costs of \$5.0 million related to unscheduled terminations and transitions and \$0.3 million of other costs, partially offset by an increase of \$1.7 million related to scheduled terminations and transitions for the nine months ended September 30, 2016 versus the same period in 2015.

Other income (expense)

Gain on sale of flight equipment decreased by \$28.1 million, to \$14.9 million for the nine months ended September 30, 2016, versus gains of \$43.0 million for the same period in 2015. During the nine months ended September 30, 2016, we recorded gains totaling \$26.7 million that were partially offset by losses totaling \$11.8 million, including a loss of \$5.2 million for a wide-body aircraft’s lease extension classified as a sales-type lease. During the nine months ended September 30, 2015, we recorded gains totaling \$44.6 million and a loss of \$1.6 million.

Income tax provision

Our provision for income taxes for the nine months ended September 30, 2016 and 2015 was \$8.8 million and \$12.0 million, respectively. Income taxes have been provided based on the applicable tax laws and rates of those countries in which operations are conducted and income is earned, primarily Ireland, Singapore and the United States. The decrease in our income tax provision of approximately \$3.3 million for the nine months ended September 30, 2016 as compared to the same period in 2015 was primarily attributable to changes in operating income subject to tax in Ireland, Singapore, the United States and other jurisdictions.

All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically





are not subject to U.S. federal, state or local income taxes unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. The aircraft owning subsidiaries resident in Ireland, Mauritius and Singapore are subject to tax in those respective jurisdictions.

We have a U.S. based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes. We also have Ireland and Singapore based subsidiaries which provide management services to our non-U.S. subsidiaries and are subject to tax in those respective jurisdictions.

The Company received an assurance from the Bermuda Minister of Finance that it would be exempted from local income, withholding and capital gains taxes until March 2035. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily the United States and Ireland.

#### Other comprehensive income

	Nine Months Ended September 30,	
	2016	2015
	(Dollars in thousands)	
Net income	\$ 83,729	\$ 71,088
Net change in fair value of derivatives, net of tax expense of \$0 and \$26, respectively	(1 )	708
Derivative loss reclassified into earnings	9,074	19,349
Total comprehensive income	\$ 92,802	\$ 91,145

Other comprehensive income increased by \$1.7 million for the nine months ended September 30, 2016, as a result of a \$12.6 million increase in net income and a decrease of \$10.3 million in amortization of deferred net losses reclassified into earnings related to terminated interest rate derivatives and a \$0.7 million decrease in gain from the change in fair value of interest rate derivatives compared to the same period in 2015.

#### Summary of Recoverability Assessment and Other Impairments

##### Recoverability Assessment

We completed our annual recoverability assessment of narrow-body aircraft in the third quarter. We also performed aircraft-specific analyses where there were changes in circumstances, such as approaching lease expirations.

The recoverability assessment is a comparison of the carrying value of each aircraft to its undiscounted expected future cash flows. We develop the assumptions used in the recoverability assessment, including those relating to current and future demand for each aircraft type, based on management's experience in the aircraft leasing industry, as well as information received from third-party sources. Estimates of the undiscounted cash flows for each aircraft type are impacted by changes in contracted and future expected lease rates, residual values, expected scrap values, economic conditions and other factors.

In our third quarter 2016 assessment, we reduced economic lives and residuals for all six older Boeing 757-200 aircraft as we intend to sell these aircraft at lease end. As a result, during the three months ended September 30, 2016, we recorded impairment charges totaling \$2.2 million relating to two of these aircraft and impairment losses totaling \$2.6 million relating to three of these aircraft held as finance leases.

During the second quarter of 2016, we completed our annual recoverability assessment of wide-body and freighter aircraft. As a result of this assessment, we reduced forecasted cash flows for older Airbus A330 aircraft to reflect lower rental expectations given weak demand and increased competition from newer units. As a result, during the three months ended June 30, 2016, we recorded impairment charges totaling \$11.7 million and maintenance revenue of \$4.0 million relating to one sixteen year old Airbus A330-200 approaching lease expiry.

In our 2015 assessment, we reduced forecasted future cash flows for our six Boeing 747-400 converted freighter aircraft not subject to sales agreements, all of which were more than twenty years old. Our new forecast reflected the persisting glut of supply in the air cargo market resulting from weak growth in demand combined with the growth in

capacity arising from new production air freighters and higher belly capacity in latest generation wide-body passenger aircraft. In addition to these market-wide impacts, our older freighters were affected specifically by the imposition of age limits in certain countries and by lower utilization levels.

As a result, we determined that each of our older converted freighter aircraft was on its last lease, and we reduced our residual value assumptions for these aircraft and expected to scrap them following lease expiry. During the third quarter of 2015, we therefore impaired four of these aircraft, which had an aggregate net book value as of August 31, 2015 of \$115.9 million, writing down their book values by a total of \$34.6 million, with a fair value date of September 1, 2015. For one of these aircraft, we recorded maintenance revenue of \$5.9 million, as we no longer planned to reinvest these funds.

#### Other Impairments

During the three months ended September 30, 2016, we reduced forecasted cash flows for three Boeing 747-400 freighter aircraft due to a change in planned engine maintenance events. These three aircraft are nearing the end of their economic lives and leases. As a result, we recorded impairment charges totaling \$5.5 million, maintenance revenue of \$5.6 million and reversed lease incentives of \$2.4 million.

Also during the three months ended September 30, 2016, we impaired one Airbus A321-200 aircraft for which we had a sales agreement, resulting in an impairment of \$1.7 million. This aircraft was classified as Held for sale in Other assets at September 30, 2016 and sold for its recorded value in October 2016.

During the three months ended June 30, 2016, we entered into an agreement to sell two older Boeing 747-400 freighter aircraft to the lessee resulting in an impairment of \$5.1 million. These two aircraft were classified as Held for sale at June 30, 2016 in Other assets and were subsequently sold in July 2016.

In September 2015, Malaysian Airline System (“MAS”) informed us that it was effectively rejecting the lease on our Boeing 777-200ER aircraft as part of its restructuring. This aircraft, which was manufactured in 1998, was the only one of its type in our fleet and the only aircraft we had on lease to MAS. We repossessed it in October 2015. We reduced the carrying value of this aircraft to our best estimate of scrap value. This write-down resulted in an impairment of \$37.8 million, partially offset by \$1.2 million of other revenue from a letter of credit we drew following the lease rejection. This aircraft was sold during the second quarter of 2016.

Also in September 2015, we modified the lease agreement with respect to one Airbus A321-200 aircraft. We elected not to reinvest in certain major maintenance events during the lease term, and the lessee agreed to release its rights to certain maintenance payments. As a result, we recorded an impairment of \$6.1 million and maintenance revenue of \$7.1 million for this aircraft.

In the second quarter of 2015, we impaired two McDonnell Douglas MD-11 freighter aircraft and one Boeing 737-800 aircraft and recorded impairment charges totaling \$24.0 million and maintenance revenue of \$18.2 million.

Other than the aircraft discussed above, management believes that the net book value of each of our wide-body and freighter aircraft is currently supported by the estimated future undiscounted cash flows expected to be generated by that aircraft, and accordingly, no other aircraft were impaired as a consequence of this recoverability assessment.

However, if our estimates or assumptions change, we may revise our cash flow assumptions and record future impairment charges. While we believe that the estimates and related assumptions used in the recoverability assessment are appropriate, actual results could differ from those estimates.

#### Aircraft Monitoring List

At September 30, 2016, we considered six freighter aircraft and six passenger aircraft with a total net book value of \$408.6 million to be more susceptible to failing our recoverability assessments due to their sensitivity to changes in contractual cash flows, future cash flow estimates and aircraft residual or scrap values.

The majority of the aircraft on the Monitoring List by net book value are freighters. Four of the freighters are Boeing 747-400 models that were converted from passenger to cargo configuration and are in excess of twenty years old. It is assumed they will be sold for scrap as their leases expire over the next two years.

The other two freighter aircraft on the Monitoring List are Boeing 747-400 extended range “factory” freighter models that are less than ten years old. Our useful life assumptions for these aircraft were reduced during our Fleet Review two years ago. These aircraft were recently added to the Monitoring List. We expect rental levels will drop from current levels over the next two years once the current leases expire or rentals are reset.

The six passenger aircraft on the Monitoring List consist of three twenty-year old Boeing 757 aircraft, which we anticipate selling as they come off lease during the next eighteen months; the other three aircraft are older Airbus A330-200s



that are either on lease or subject to a lease commitment. Future rental assumptions for these Airbus A300-200 aircraft were reduced as part of the Fleet Review completed during the second quarter of 2016.

**RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS**

See Note 1 - "Summary of Significant Accounting Policies – Organization and Basis of Presentation" in the Notes to Unaudited Consolidated Financial Statements above.

**RECENTLY UNADOPTED ACCOUNTING PRONOUNCEMENTS**

See Note 1 - "Summary of Significant Accounting Policies – Recent Accounting Pronouncements" in the Notes to Unaudited Consolidated Financial Statements above.

## LIQUIDITY AND CAPITAL RESOURCES

Our business is very capital intensive, requiring significant investments in order to expand our fleet and to maintain and improve our existing portfolio. Our operations generate a significant amount of cash, primarily from lease rentals and maintenance collections. We have also met our liquidity and capital resource needs by utilizing several sources over time, including:

- various forms of borrowing secured by our aircraft, including bank term facilities, limited recourse securitization financings, and ECA-backed financings for new aircraft acquisitions;
- unsecured indebtedness, including our current Revolving Credit Facility and Senior Notes;
- sales of common shares; and
- asset sales.

Going forward, we expect to continue to seek liquidity from these sources and other sources, subject to pricing and conditions we consider satisfactory.

During the first nine months of 2016, we met our liquidity and capital resource needs with \$367.4 million of cash flow from operations, \$500.0 million in gross proceeds from the issuance of our Senior Notes due 2023, a \$120.0 million term loan, \$372.8 million in full-recourse term financing and \$488.7 million of cash from aircraft sales.

In addition, we increased the Revolving Credit Facility from \$600.0 million to \$675.0 million, and we extended the maturity of that facility by one year to May 2020.

As of September 30, 2016, the weighted-average maturity of our secured and unsecured debt financings was 3.9 years and we are in compliance with all applicable covenants.

We believe that cash on hand, payments received from lessees and other funds generated from operations, secured borrowings for aircraft, borrowings under our Revolving Credit Facility and other borrowings and proceeds from future aircraft sales will be sufficient to satisfy our liquidity and capital resource needs over the next twelve months.

Our liquidity and capital resource needs include payments due under our aircraft purchase obligations, required principal and interest payments under our long-term debt facilities, expected capital expenditures, lessee maintenance payment reimbursements and lease incentive payments over the next twelve months.

## Cash Flows

	Nine Months Ended	
	September 30,	
	2016	2015
	(Dollars in thousands)	
Net cash flow provided by operating activities	\$367,413	\$408,470
Net cash flow used in investing activities	(378,533 )	(713,471 )
Net cash flow provided by financing activities	511,463	284,386

## Operating Activities:

Cash flow provided by operations was \$367.4 million and \$408.5 million for the nine months ended September 30, 2016 and 2015, respectively. The decrease in cash flow provided by operations of approximately \$41.1 million for the nine months ended September 30, 2016 versus the same period in 2015 was primarily a result of:

- a \$25.4 million decrease in cash from maintenance revenue;
  - a \$12.0 million increase in cash paid for interest;
- a \$10.1 million decrease in cash from lease rentals, net of finance and sales-type leases; and
  - a \$3.2 million increase in cash paid for taxes.

These outflows were partially offset by:

- a \$9.5 million decrease in cash from working capital; and
- a \$3.6 million decrease in cash paid for maintenance.

## Investing Activities:

Cash flow used in investing activities was \$378.5 million and \$713.5 million for the nine months ended September 30, 2016 and 2015, respectively. The net decrease in cash flow used in investing activities of \$334.9 million for the nine months ended September 30, 2016 versus the same period in 2015 was primarily a result of:

- a \$242.3 million decrease in the acquisition and improvement of flight equipment;
- a \$145.7 million increase in proceeds from the sale of flight equipment; and
- a \$17.0 million increase in restricted cash and cash equivalents related to the sale of flight equipment.

These outflows were offset by:

- a \$47.2 million increase in net investments in finance and sales-type leases;
- a \$12.7 million increase in unconsolidated equity method investment in 2016; and
- a \$9.6 million net decrease in aircraft purchase deposits received.

## Financing Activities:

Cash flow provided by financing activities was \$511.5 million and \$284.4 million for the nine months ended September 30, 2016 and 2015, respectively. The increase in cash flow provided by financing activities of \$227.1 million for the nine months ended September 30, 2016 versus the same period in 2015 was a result of:

- a \$199.4 million increase in proceeds from secured and unsecured financings;
- a \$59.2 million decrease in securitization and term debt financing repayments; and
- a \$12.5 million increase in restricted cash and cash equivalents related to financing activities.

These outflows were offset by:

- a \$34.6 million increase in shares repurchased;
- a \$5.1 million increase in deferred financing costs; and
- a \$3.1 million increase in dividends paid.

## Debt Obligations

For complete information on our debt obligations, please refer to Note 7 - "Secured and Unsecured Debt Financings" in the Notes to Unaudited Consolidated Financial Statements above.

## Contractual Obligations

Our contractual obligations consist of principal and interest payments on debt, payments on interest rate derivatives, other aircraft acquisition agreements and rent payments pursuant to our office leases. Total contractual obligations increased to \$6.87 billion at September 30, 2016 from \$6.30 billion at December 31, 2015 due primarily to an increase in borrowings and interest payments as a result of the closing of our Senior Notes due 2023 in March 2016, funding the DBJ Term Loan in April 2016 and funding the ACS 2016 Bank Financing during the second and third quarters of 2016, partially offset by the repayment of our Revolving Credit Facility, the prepayment of Securitization No. 2 and the amortization of our other financings.

The following table presents our actual contractual obligations and their payment due dates as of September 30, 2016:

Contractual Obligations	Payments Due by Period as of September 30, 2016				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
	(Dollars in thousands)				
Principal payments:					
Senior Notes due 2017 - 2023	\$3,200,000	\$500,000	\$400,000	\$1,300,000	\$1,000,000
DBJ Term Loan	120,000	—	120,000	—	—
Revolving Credit Facility	—	—	—	—	—
ECA Financings	315,687	42,209	88,974	95,415	89,089
Bank Financings	970,525	90,735	240,731	158,861	480,198
Total principal payments	4,606,212	632,944	849,705	1,554,276	1,569,287
Interest payments on debt obligations <sup>(1)</sup>	933,999	232,191	369,333	231,112	101,363
Office leases <sup>(2)</sup>	4,619	1,952	1,158	447	1,062
Purchase obligations <sup>(3)</sup>	1,322,989	400,207	399,599	523,183	—
Total	\$6,867,819	\$1,267,294	\$1,619,795	\$2,309,018	\$1,671,712

(1) Future interest payments on variable rate, LIBOR-based debt obligations are estimated using the interest rate in effect at September 30, 2016.

(2) Represents contractual payment obligations for our office leases in Stamford, Connecticut; Dublin, Ireland and Singapore.

At September 30, 2016, we had commitments to acquire 36 aircraft for \$1.32 billion, including 25 new E-Jet E-2 aircraft from Embraer S.A. These amounts include estimates for pre-delivery deposits, contractual price escalation and other adjustments. As of October 28, 2016, we have commitments to acquire 37 aircraft for \$1.36 billion.

## Capital Expenditures

From time to time, we make capital expenditures to maintain or improve our aircraft. These expenditures include the cost of major overhauls necessary to place an aircraft in service and modifications made at the request of lessees. For the nine months ended September 30, 2016 and 2015, we incurred a total of \$27.0 million and \$31.5 million, respectively, of capital expenditures (including lease incentives) related to the acquisition and improvement of aircraft.

As of September 30, 2016, the weighted average age by net book value of our aircraft was approximately 7.6 years. In general, the costs of operating an aircraft, including maintenance expenditures, increase with the age of the aircraft. Our lease agreements call for the lessee to be primarily responsible for maintaining the aircraft. We may incur additional maintenance and modification costs in the future in the event we are required to remarket an aircraft or a lessee fails to meet its maintenance obligations under the lease agreement. These maintenance reserves are paid by the lessee to provide for future maintenance events. Provided a lessee performs scheduled maintenance of the aircraft, we are required to reimburse the lessee for scheduled maintenance payments. In certain cases, we are also required to make lessor contributions, in excess of amounts a lessee may have paid, towards the costs of maintenance events



performed by or on behalf of the lessee.

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Actual maintenance payments to us by lessees in the future may be less than projected as a result of a number of factors, including defaults by the lessees. Maintenance reserves may not cover the entire amount of actual maintenance expenses incurred and, where these expenses are not otherwise covered by the lessees, there can be no assurance that our operational cash flow and maintenance reserves will be sufficient to fund maintenance requirements, particularly as our aircraft age. See Item 1A. “Risk Factors - Risks Related to Our Business - Risks related to our leases - If lessees are unable to fund their maintenance obligations on our aircraft, we may incur increased costs at the conclusion of the applicable lease” in our 2015 Annual Report on Form 10-K.

#### Off-Balance Sheet Arrangements

We entered into two joint venture arrangements in order to help expand our base of new business opportunities. None of these joint ventures qualifies for consolidated accounting treatment. The assets and liabilities of these entities are not included in our Consolidated Balance Sheets and we record our net investment under the equity method of accounting. See Note 5 - “Unconsolidated Equity Method Investment” in the Notes to Unaudited Consolidated Financial Statements above.

We hold a 30% equity interest in our joint venture with an affiliate of Teachers’ and a 25% equity interest in our joint venture with the IJB Leasing Co., Ltd., a Japanese general leasing company which is part of the Mizuho Financial Group. At September 30, 2016, the net book value of our two joint ventures’ eleven aircraft was approximately \$629 million.

#### Foreign Currency Risk and Foreign Operations

At September 30, 2016, all of our leases are payable to us in U.S. dollars. However, we incur Euro and Singapore dollar-denominated expenses in connection with our subsidiaries in Ireland and Singapore. For the nine months ended September 30, 2016, expenses, such as payroll and office costs, denominated in currencies other than the U.S. dollar aggregated approximately \$12.7 million in U.S. dollar equivalents and represented approximately 27% of total selling, general and administrative expenses. Our international operations are a significant component of our business strategy and permit us to more effectively source new aircraft, service the aircraft we own and maintain contact with our lessees. Therefore, our international operations and our exposure to foreign currency risk will likely increase over time. Although we have not yet entered into foreign currency hedges because our exposure to date has not been significant, if our foreign currency exposure increases, we may enter into hedging transactions in the future to mitigate this risk. For the nine months ended September 30, 2016 and 2015, we incurred insignificant net gains and losses on foreign currency transactions.

#### Hedging

For complete information on our derivative instruments, please refer to Note 16 - “Accumulated Other Comprehensive Loss” in the Notes to Consolidated Financial Statements above.

#### Management’s Use of EBITDA and Adjusted EBITDA

We define EBITDA as income (loss) from continuing operations before income taxes, interest expense, and depreciation and amortization. We use EBITDA to assess our consolidated financial and operating performance, and we believe this non-U.S. GAAP measure is helpful in identifying trends in our performance.

This measure provides an assessment of controllable expenses and affords management the ability to make decisions which are expected to facilitate meeting current financial goals, as well as achieving optimal financial performance. It provides an indicator for management to determine if adjustments to current spending decisions are needed.

EBITDA provides us with a measure of operating performance because it assists us in comparing our operating performance on a consistent basis as it removes the impact of our capital structure (primarily interest charges on our outstanding debt) and asset base (primarily depreciation and amortization) from our operating results. Accordingly, this metric measures our financial performance based on operational factors that management can impact in the short-term, namely the cost structure, or expenses, of the organization. EBITDA is one of the metrics used by senior management and the Board of Directors to review the consolidated financial performance of our business.

We define Adjusted EBITDA as EBITDA (as defined above) further adjusted to give effect to adjustments required in calculating covenant ratios and compliance as that term is defined in the indenture governing our senior unsecured notes. Adjusted EBITDA is a material component of these covenants.



The table below shows the reconciliation of net income to EBITDA and Adjusted EBITDA for the three and nine months ended September 30, 2016 and 2015:

	Three Months Ended		Nine Months Ended	
	September 30, 2016	2015	September 30, 2016	2015
	(Dollars in thousands)			
Net income (loss)	\$27,437	\$(13,989 )	\$83,729	\$71,088
Depreciation	76,201	85,324	227,918	237,538
Amortization of net lease discounts and lease incentives	521	2,113	5,419	10,288
Interest, net	61,797	60,381	188,490	184,063
Income tax provision	2,458	2,709	8,782	12,037
EBITDA	168,414	136,538	514,338	515,014
Adjustments:				
Impairment of aircraft	10,462	78,403	27,185	102,358
Non-cash share-based payment expense	2,059	1,424	5,796	3,981
(Gain) loss on mark-to-market of interest rate derivative contracts	210	(54 )	141	(220 )
Adjusted EBITDA	\$181,145	\$216,311	\$547,460	\$621,133

#### Management's Use of Adjusted Net Income ("ANI")

Management believes that ANI, when viewed in conjunction with the Company's results under U.S. GAAP and the below reconciliation, provides useful information about operating and period-over-period performance and additional information that is useful for evaluating the underlying operating performance of our business without regard to periodic reporting elements related to interest rate derivative accounting, changes related to refinancing activity and non-cash share-based payment expense.

The table below shows the reconciliation of net income to ANI for the three and nine months ended September 30, 2016 and 2015:

	Three Months		Nine Months	
	Ended September 30, 2016	2015	Ended September 30, 2016	2015
	(Dollars in thousands)			
Net income (loss)	\$27,437	\$(13,989)	\$83,729	\$71,088
Loan termination fee <sup>(1)</sup>	—	—	1,509	—
Ineffective portion and termination of hedges <sup>(1)</sup>	—	215	—	509
(Gain) loss on mark-to-market of interest rate derivative contracts <sup>(2)</sup>	210	(54 )	141	(220 )
Write-off of deferred financing fees <sup>(1)</sup>	—	—	1,972	—
Non-cash share-based payment expense <sup>(3)</sup>	2,059	1,424	5,796	3,981
Term Financing No. 1 hedge loss amortization charges <sup>(1)</sup>	—	—	—	4,401
Securitization No. 1 hedge loss amortization charges <sup>(1)</sup>	—	2,725	4,855	8,248
Adjusted net income (loss)	\$29,706	\$(9,679 )	\$98,002	\$88,007

(1) Included in Interest, net.

(2) Included in Other income (expense).

(3) Included in Selling, general and administrative expenses.

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Weighted-average shares:				
Common shares outstanding	77,989,933	80,566,400	78,230,011	80,565,754
Restricted common shares	680,249	645,427	646,299	604,179
Total weighted-average shares	78,670,182	81,211,827	78,876,310	81,169,933
	Three Months Ended September 30,		Nine Months Ended September 30,	
Percentage of weighted-average shares:	2016	2015	2016	2015
Common shares outstanding	99.14 %	99.21 %	99.18 %	99.26 %
Restricted common shares <sup>(1)</sup>	0.86 %	0.79 %	0.82 %	0.74 %
Total percentage of weighted-average shares	100.00 %	100.00 %	100.00 %	100.00 %
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Weighted-average common shares outstanding – Basic	77,989,933	80,566,400	78,230,011	80,565,754
Effect of dilutive shares <sup>(2)</sup>	32,235	—	35,804	—
Weighted average common shares outstanding – Diluted	78,022,168	80,566,400	78,265,815	80,565,754
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Adjusted net income (loss) allocation:				
Adjusted net income (loss)	\$29,706	\$(9,679)	\$98,002	\$88,007
Less: Distributed and undistributed earnings allocated to restricted common shares <sup>(1)</sup>	(257 )	—	(803 )	(655 )
Adjusted net income (loss) allocable to common shares – Basic and Diluted	\$29,449	\$(9,679)	\$97,199	\$87,352
Adjusted net income (loss) per common share – Basic and Diluted	\$0.38	\$(0.12 )	\$1.24	\$1.08

(1) For the three months ended September 30, 2016, distributed and undistributed earnings to restricted shares are 0.86% of net income. For the nine months ended September 30, 2016 and 2015, distributed and undistributed earnings to restricted shares are 0.82% and 0.74%, respectively, of net income. The amount of restricted share forfeitures for all periods present is immaterial to the allocation of distributed and undistributed earnings.

(2) For the three and nine months ended September 30, 2016, dilutive shares represented contingently issuable shares related to the Company's PSUs. For the three and nine months ended September 30, 2015, we had no dilutive shares.

#### Limitations of EBITDA, Adjusted EBITDA and ANI

An investor or potential investor may find EBITDA, Adjusted EBITDA and ANI important measures in evaluating our performance, results of operations and financial position. We use these non-U.S. GAAP measures to supplement our U.S. GAAP results in order to provide a more complete understanding of the factors and trends affecting our business.

EBITDA, Adjusted EBITDA and ANI have limitations as analytical tools and should not be viewed in isolation or as substitutes for U.S. GAAP measures of earnings (loss). Material limitations in making the adjustments to our earnings (loss) to calculate EBITDA, Adjusted EBITDA and ANI, and using these non-U.S. GAAP measures as compared to U.S. GAAP net income (loss), income (loss) from continuing operations and cash flows provided by or used in operations, include:

depreciation and amortization, though not directly affecting our current cash position, represent the wear and tear and/or reduction in value of our aircraft, which affects the aircraft's availability for use and may be indicative of future needs for capital expenditures;

the cash portion of income tax (benefit) provision generally represents charges (gains), which may significantly affect our financial results;

elements of our interest rate derivative accounting may be used to evaluate the effectiveness of our hedging policy; hedge loss amortization charges related to Term Financing No. 1 and Securitization No. 1; and adjustments required in calculating covenant ratios and compliance as that term is defined in the indenture governing our senior unsecured notes.

EBITDA, Adjusted EBITDA and ANI are not alternatives to net income (loss), income (loss) from operations or cash flows provided by or used in operations as calculated and presented in accordance with U.S. GAAP. You should not rely on these non-U.S. GAAP measures as a substitute for any such U.S. GAAP financial measure. We strongly urge you to review the reconciliations to U.S. GAAP net income (loss), along with our consolidated financial statements included elsewhere in this report. We also strongly urge you to not rely on any single financial measure to evaluate our business. In addition, because EBITDA, Adjusted EBITDA and ANI are not measures of financial performance under U.S. GAAP and are susceptible to varying calculations, EBITDA, Adjusted EBITDA and ANI as presented in this report, may differ from and may not be comparable to similarly titled measures used by other companies.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest rate risk is the exposure to loss resulting from changes in the level of interest rates and the spread between different interest rates. These risks are highly sensitive to many factors, including U.S. monetary and tax policies, U.S. and international economic factors and other factors beyond our control. We are exposed to changes in the level of interest rates and to changes in the relationship or spread between interest rates. Our primary interest rate exposures relate to our lease agreements, floating rate debt obligations and interest rate derivatives. Rent payments under our aircraft lease agreements typically do not vary during the term of the lease according to changes in interest rates. However, our borrowing agreements generally require payments based on a variable interest rate index, such as LIBOR. Therefore, to the extent our borrowing costs are not fixed, increases in interest rates may reduce our net income by increasing the cost of our debt without any corresponding increase in rents or cash flow from our securities. Changes in interest rates may also impact our net book value as our interest rate derivatives are periodically marked-to-market through shareholders' equity. Generally, we are exposed to loss on our fixed pay interest rate derivatives to the extent interest rates decrease below their contractual fixed rate.

The relationship between spreads on derivative instruments may vary from time to time, resulting in a net aggregate book value increase or decrease. Changes in the general level of interest rates can also affect our ability to acquire new investments and our ability to realize gains from the settlement of such assets.

#### Sensitivity Analysis

The following discussion about the potential effects of changes in interest rates is based on a sensitivity analysis, which models the effects of hypothetical interest rate shifts on our financial condition and results of operations. Although we believe a sensitivity analysis provides the most meaningful analysis permitted by the rules and regulations of the SEC, it is constrained by several factors, including the necessity to conduct the analysis based on a single point in time and by the inability to include the extraordinarily complex market reactions that normally would arise from the market shifts modeled. Although the following results of a sensitivity analysis for changes in interest rates may have some limited use as a benchmark, they should not be viewed as a forecast. This forward-looking disclosure also is selective in nature and addresses only the potential interest expense impacts on our financial instruments and, in particular, does not address the mark-to-market impact on our interest rate derivatives. It also does not include a variety of other potential factors that could affect our business as a result of changes in interest rates. A hypothetical 100-basis point increase/decrease in our variable interest rates would increase/decrease the minimum contracted rentals on our portfolio as of September 30, 2016 by \$2.9 million and \$3.4 million, respectively, over the next twelve months. As of September 30, 2016, a hypothetical 100-basis point increase/decrease in our variable interest rate on our borrowings would result in an interest expense increase/decrease of \$8.0 million and \$7.2 million, respectively, net of amounts received from our interest rate derivatives, over the next twelve months. In September 2016, we purchased an interest rate cap for \$2,283 to hedge approximately 70% of our floating rate interest exposure. The interest rate cap is set at 2% and has a starting notional balance of \$430,000 and reduces over time to \$215,000. The cap matures in September 2021.

#### ITEM 4. CONTROLS AND PROCEDURES

##### Management's Evaluation of Disclosure Controls and Procedures

The term "disclosure controls and procedures" is defined in Exchange Act Rules 13a-15(e) and 15d-15(e). This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") as appropriate, to allow timely decisions regarding required disclosure. An evaluation was performed under the supervision and with the participation of the Company's management, including the CEO and CFO, of the effectiveness of the Company's disclosure controls and procedures as of September 30, 2016. Based on that evaluation, the Company's management, including the CEO and CFO, concluded that the Company's disclosure controls and procedures were effective as of September 30, 2016.

##### Changes in Internal Control over Financial Reporting

There were no changes in the Company's internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f), that occurred during the quarter ended September 30, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.



## PART II. — OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

The Company is not a party to any material legal or adverse regulatory proceedings.

## ITEM 1A. RISK FACTORS

There have been no material changes to the disclosure related to the risk factors described in our Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2015.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## Issuer Purchases of Equity Securities

In February 2016, our Board of Directors authorized the repurchase of up to \$100.0 million of the Company's common shares. During the third quarter of 2016, we purchased our common shares as follows:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>(1)</sup>	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(1)</sup>
	(Dollars in thousands, except per share amounts)			
July 1 through July 31	143,639	\$ 18.93	143,639	\$ 96,656
August 1 through August 31	—	—	—	96,656
September 1 through September 30	—	—	—	96,656
Total	143,639	\$ 18.98	143,639	\$ 96,656

<sup>(1)</sup> Under our current repurchase program, we have repurchased an aggregate of 176,574 common shares at an aggregate cost of \$3.3 million, including commissions.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit No.	Description of Exhibit
3.1	Memorandum of Association (incorporated by reference to Exhibit 3.1 to the Company's Registration Statement on Form S-1 (Amendment No. 2) (No. 333-134669) filed on July 25, 2006).
3.2	Amended Bye-laws (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form S-3 (No. 333-182242) filed on June 20, 2012).
4.1	Specimen Share Certificate (incorporated by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-1 (Amendment No. 2) (No. 333-134669) filed on July 25, 2006).
4.2	Indenture, dated as of April 4, 2012, by and between Aircastle Limited and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on April 5, 2012).
4.3	Indenture, dated as of November 30, 2012, by and between Aircastle Limited and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed with the SEC on November 30, 2012).
4.4	Amended and Restated Shareholder Agreement, dated as of February 18, 2015, by and between Aircastle Limited and Marubeni Corporation (incorporated by reference to Exhibit 4.8 to the Company's Quarterly Report on Form 10-Q filed on May 6, 2015).
4.5	Amendment No. 1 to the Amended and Restated Shareholder Agreement, dated as of September 23, 2016, by and among Aircastle Limited, Marubeni Corporation, and Marubeni Aviation Holding Coöperatief U.A. (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on September 26, 2016).
4.6	Indenture, dated as of December 5, 2013, by and between Aircastle Limited and Wells Fargo Bank, National Association, as trustee Citigroup Global Markets, Inc., Goldman, Sachs & Co., J.P. Morgan Securities LLC and RBC Capital Markets, LLC (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on December 6, 2013).
4.7	First Supplemental Indenture, dated as of December 5, 2013, by and between Aircastle Limited and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.2 to the Company's Current Report on Form 8-K filed on December 6, 2013).
4.8	Second Supplemental Indenture, dated as of March 26, 2014, by and between Aircastle Limited and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on March 26, 2014).
4.9	Third Supplemental Indenture, dated as of January 15, 2015, by and between Aircastle Limited and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on January 15, 2015).
4.10	Fourth Supplemental Indenture, dated as of March 24, 2016, by and between Aircastle Limited and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on March 24, 2016).

- 10.1 Letter Agreement, dated as of October 4, 2016, by and between Aircastle Advisor LLC and Aaron Dahlke (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on October 7, 2016).
- 31.1 Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002. \*
- 31.2 Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002. \*
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \*
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \*
- 99.1 Owned Aircraft Portfolio at September 30, 2016. \*

101 The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2016, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets as of September 30, 2016 and December 31, 2015; (ii) Consolidated Statements of Income for the three and nine months ended September 30, 2016 and 2015; (iii) Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2016 and 2015; (iv) Consolidated Statements of Cash Flows for the three and nine months ended September 30, 2016 and 2015; and (v) Notes to Unaudited Consolidated Financial Statements. \*

\*Filed herewith.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: November 1, 2016

AIRCASTLE LIMITED

(Registrant)

By: /s/ Aaron Dahlke

Aaron Dahlke

Chief Accounting Officer and Authorized Officer