C

AIR CANADA

2000 Annual Report

Building Merging Innovating

Destinations served by Air Canada

Direct and Codeshare Service

CANADA

- Bagotville
- Baie Comeau
- Baker Lake*
- Bathurst
- Blanc Sablon*
- Brochet*
- Calgary
- Cambridge Bay*
- Campbell River
- Castlegar
- Charlottetown
- Chesterfield Inlet*
- Chibougamau*
- Chisasibi*
- Churchill*
- Comox
- Coral Harbour*
- Cranbrook
- Dawson Creek*
- Deer Lake
- Dryden*
- Edmonton
- Eskimo Point*
- Flin Flon*
- Ft. McMurray
- Fredericton
- Ft. Nelson
- Ft. St. John
- Gander
- Gaspé
- Gillam*
- Goose Bay
- Grande Prairie
- Halifax
- Harrington Harbour*
- Havre St. Pierre*
- High Level
- Îles de la Madeleine
- Inuvik*
- Iqaluit*
- Kamloops
- Kelowna
- Kingston
- Kuujjuarapik*
- La Grande*
- Lac Brochet*
- Lethbridge
- Lloydminster*
- London
- Lynn Lake*
- Medicine Hat*
- Moncton
- Mont-Joli
- Montréal
- Nanaimo
- Natashquan*
- North Bay
- Ottawa
- Pakuashipi*
- Peace River
- Penticton
- Port Menier*
- Prince George
- Prince Rupert
- Québec
- Quesnel
- Rainbow Lake
- Rankin Inlet*
- Regina
- Repulse Bay*
- Roberval*
- Rouyn-Noranda
- Saint John, NB
- Sandspit
- Sarnia
- Saskatoon
- Sault Ste. Marie
- Schefferville*
- Sept-Îles
- Smithers
- St. John's, NF
- St. Leonard
- Stephenville
- Sudbury
- Sydney
- Tadoule Lake*
- Terrace
- The Pas*
- Thompson
- Thunder Bay
- Timmins
- Toronto
- Val d'Or
- Vancouver
- Victoria
- Wabush
- Whale Cove*
- Whitehorse
- Williams Lake
- Windsor
- Winnipeg
- Yarmouth
- Yellowknife*

UNITED STATES

- Albany*
- Albuquerque*
- Allentown
- Atlanta
- Austin*
- Baltimore
- Billings*
- Boise*
- Boston
- Buffalo*
- Burbank*
- Burlington*
- Cedar Rapids*
- Charleston, SC*
- Charleston, WV*
- Charlotte, NC
- Charlottesville*
- Chicago
- Cincinnati*
- Cleveland
- Colorado Springs*
- Columbia*
- Columbus
- Dallas / Fort Worth
- Dayton*
- Denver
- Des Moines*
- Detroit
- Eugene*
- Ft. Lauderdale
- Fort Myers
- Fort Wayne*
- Grand Rapids*
- Greensboro*
- Greenville*
- Hampton*
- Harrisburg
- Hartford
- Honolulu
- Houston
- Indianapolis*
- Jacksonville*
- Kahului
- Kansas City
- Knoxville*
- Las Vegas
- Lincoln*
- Los Angeles
- Louisville*
- Lynchburg*
- Manchester*
- Memphis*
- Miami
- Milwaukee
- Minneapolis
- Mobile*
- Myrtle Beach**
- Nashville
- New Orleans
- New York
- Newark
- Norfolk*
- Oklahoma City*
- Omaha*
- Ontario*
- Orlando
- Palm Springs*
- Philadelphia
- Phoenix
- Pittsburgh
- Portland, ME
- Portland, OR
- Providence
- Raleigh/Durham
- Reno*
- Richmond
- Roanoke*
- Rochester*
- Sacramento*
- Saginaw*
- Salt Lake City*
- San Diego
- San Francisco
- San Jose
- Santa Ana*
- Savannah*
- Seattle
- Spokane*
- St. Louis
- Syracuse*
- Tampa
- Tucson*
- Tulsa*
- Washington, D.C.
- West Palm Beach
- Wichita*

INTERNATIONAL

- Aalborg*
- Aarhus*
- Abu Dhabi*
- Acapulco*
- Amman*
- Amsterdam*
- Antigua
- Athens*
- Auckland*
- Beijing
- Barbados
- Belfast*
- Bergen*
- Berlin*
- Bermuda
- Bremen*
- Brussels*
- Bucharest*
- Budapest*
- Buenos Aires
- Cancun*
- Cologne*
- Copenhagen
- Dresden*
- Dubai*
- Dusseldorf*
- Edinburgh*
- Fort-de-France
- Frankfurt
- Glasgow
- Gothenburg*
- Guadalajara*
- Hamburg*
- Hanover*
- Helsinki*
- Hong Kong
- Huatulco*
- Ixtapa*
- Jönköping*
- Karlstad*
- Kiev*
- Kingston
- Leeds / Bradford*
- Leipzig*
- Leon*
- London
- Los Cabos*
- Manchester
- Mazatlan*
- Mexico City
- Milan
- Montego Bay
- Monterrey*
- Moscow*
- Munich
- Muenster*
- Nassau
- Nagoya
- Norrköping*
- Nuremberg*
- Orebro*
- Osaka
- Oslo*
- Paris
- Pointe-à-Pitre
- Port-au-Prince
- Port of Spain
- Prague*
- Puerto Vallarta*
- Rome
- São Paulo
- San Juan**
- Seoul
- Shanghai
- Singapore*
- St. Lucia
- St. Maarten**
- St. Petersburg*
- Stavanger*
- Stockholm*
- Stuttgart*
- Sydney
- Taipei
- Teesside*
- Tel Aviv
- Tokyo
- Västerås*
- Zurich

* Served under Air Canada's designator code through codeshare agreements or Tier 3 arrangements.

** Seasonal charter service offered through Air Canada Vacations.

Together with Star Alliance and other commercial alliances, the Corporation offers air transportation to over 800 destinations around the world.

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ANNUAL MEETING

The Annual and Special Meeting of Shareholders of Air Canada will be held at 9:30 a.m. on Tuesday, May 15, 2001 at the Fairmont Winnipeg (Winnipeg Ballroom), Two Lombard Place, Winnipeg, Manitoba.

Highlights

(including Canadian Airlines from July to December 2000)

2000 financial results include Canadian Airlines from July to December and reflect integration and restructuring activities as well as dramatically increased prices for aircraft fuel.

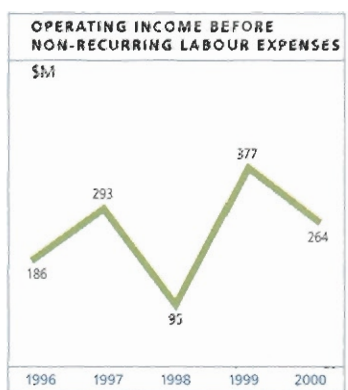
Financial [1] (Millions except per share figures)	2000	1999	Change
Operating revenues	$ 9,283	$ 6,443	44%
Operating expenses before non-recurring labour expenses	$ 9,019	$ 6,066	49%
Operating income before non-recurring labour expenses	$ 264	$ 377	
Operating income	$ 86	$ 377	
Income (loss) for the year	$ (82)	$ 140	
Operating margin before non-recurring labour expenses	2.8%	5.9%	
Cash flows from operations	$ 115	$ 680	
Cash and cash equivalents	$ 437	$ 521	
Average common shares outstanding (fully diluted) [2]	150.7	189.6	
Income (loss) for the year per common share (fully diluted) [2]	$ (0.69)	$ 0.75	
Cash flows from operations per common share (fully diluted) [2]	$ 0.87	$ 3.61	
Return on equity	(24.0)%	13.0%	
Common share, closing price (Toronto Stock Exchange)	$ 13.70	$ 10.90	

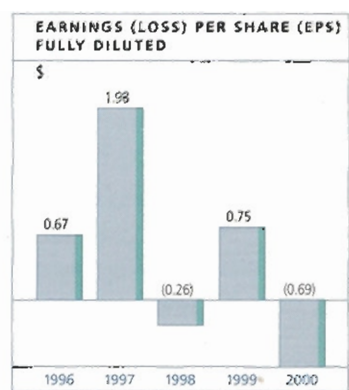
(1) 1999 restated for accounting policy changes.
(2) Per share amounts have been calculated using the weighted average number of common shares outstanding during the year.

Inclusion of Canadian Airlines, from July to December 2000, accounted for over two-thirds of the increase in traffic and capacity.

Operating Statistics Mainline Operations (Scheduled and Charter)	2000	1999	Change
Revenue passenger miles (millions)	35,658	24,242	47%
Available seat miles (millions)	49,229	33,970	45%
Passenger load factor	72.4%	71.4%	1.0 pt.
Yield per revenue passenger mile (cents)	19.5	19.8	(2)%
Operating expense per available seat mile (cents) [3]	16.3	15.9	2%
Average number of full-time equivalent employees	31,560	22,991	37%

(3) Before non-recurring labour expenses.





Including Canadian Airlines from July to December 2000.
Prior years restated for accounting policy changes.
More information on page 26.

Message from the Chairman of the Board

The merger of Canada's two major airlines is producing profound changes in the Canadian airline industry. The restructuring which it precipitated is leading Air Canada, its competitors as well as federal authorities through uncharted territory. For the Air Canada Board of Directors, this presents a new challenge in representing shareholder interests. The Board not only provides strategic direction to management and reviews the business of Air Canada, like its strategic and business plans and major capital acquisitions, but now that assessment has to be made in the context of an uncertain economy and a particularly fluid competitive environment. This means weighing multiple scenarios. Last year, the Board reviewed numerous projects related to the integration of Air Canada and Canadian Airlines involving employees, unions, technology and other actions and requiring financing or contractual commitments. Now, the completion of the integration process enables us to focus on the Corporation's strategies for leveraging shareholder value in this larger Air Canada.

To keep up with technological developments, we aslo have introduced new practices for communicating with investors. As one of Canada's most widely held public companies, it is Air Canada's goal to be at the forefront of good corporate disclosure. Our quarterly earnings conference call with analysts and investors are webcast live so that anybody can listen in, and the call is available for replay in the following days and weeks. So are major speeches by senior management to financial audiences. Detailed analyses of quarterly earnings also are posted on our website at www.aircanada.ca. These analyses contain more information than the standard earnings press releases. Texts of all speeches and other analyses containing useful information for investors are posted on our website as they are being presented, and advance notice is provided of their availability. Starting with this Annual Report, we are introducing an expanded Management Discussion & Analysis, which includes more sensitivity projections to demonstrate the likely impact on future earnings from such variable factors as crude prices, jet fuel prices, Canada-US exchange rates, Canadian and US interest rates, labour expense as well as fluctuations in overall costs or revenues per seat mile.

Finally, on behalf of the board, I would like to thank retiring director Bill James for his dedicated service through a period which has witnessed extraordinary changes for Air Canada.

John F. Fraser, O.C.
Chairman of the Board

Report from the President and Chief Executive Officer

Robert A. Milton
President and
Chief Executive Officer

It's been over a decade since Air Canada's privatization, yet in many ways the true potential of our franchise is only now being unlocked. Completing the integration of Canadian Airlines makes Air Canada a truly global airline carrying 30 million customers to over 800 destinations on five continents on our own aircraft and on services operated by our Star Alliance partners. You will witness the emergence of a more entrepreneurial corporate culture at Air Canada, employing leading edge technologies as well as new profit centre and e-commerce strategies to improve shareholder value.

But first things first. In the final weeks of 2000, a sudden slowing of business travel demand heralded a break in North America's long economic boom. We reacted decisively and before most other airlines to begin re-sizing our operations accordingly.

- There will be zero capacity growth in 2001, down from the eight per cent we planned originally.
- A number of underperforming routes and flights are being cancelled.
- With eight new widebody aircraft scheduled for delivery this year, up to eight older, less efficient widebodies will be parked, subleased or sold.
- Retirement of the narrowbody F-28s, which have the highest operating costs in the fleet, is being accelerated.
- Thirty five hundred jobs are being eliminated, primarily through a combination of voluntary separation packages, leaves of absence and attrition.

While the extent of the economic slowdown is uncertain, Air Canada is ready for any eventuality. If the economy slows further, we will tighten our belts more. If the economy begins expanding again, we can revert to growth mode very quickly. The acquisition of Canadian gives us great flexibility to reduce or redeploy more capacity without diluting our product.

Barring a major recession, I am guardedly optimistic about 2001. The current economic weakness will pressure first half earnings. However, by mid year most merger expenses will be behind us. Through the course of the year, the airline should begin to benefit from the full $700 million in annualized cost and revenue synergies expected from the integration.

A year ago, I cautioned that one-time merger costs would constrain our profitability in 2000. For a time, buoyed by record passenger demand, our income performance exceeded that conservative outlook. Through the first three quarters, operating *income – including merger and other non-recurring costs – reached a record* $478 million despite a 51 per cent rise in the per-litre cost of fuel. The economic bubble burst in the fourth quarter. While our revenue growth began slowing, growth in expenditures did not. US spot crude prices were over $36 a barrel. Our staff levels were up, reflecting record spring and summer demand, and we couldn't begin to bring down the numbers until after we had merged computer systems and started intermingling staff of both airlines in late October. So as not to complicate the computer integration, we had delayed our usual fall seat sale. Those factors combined for a fourth quarter operating loss of $245 million before one time charges and left us with a full year operating profit of $86 million – $368 million before one-time items – compared with $377 million the year before.

With the completion of Canadian's debt restructuring, Air Canada gained control of Canadian in July. Our full year 2000 net loss of $82 million on $9.3 billion in revenues reflects a full year of Air Canada results and half year for Canadian. The financial results were significantly affected by non-recurring items, which included $147 million in after tax labour and other integration expenses. Extra fuel expense amounted to $233 million after tax.

The non-recurring labour expense resulted from agreements we negotiated to allow Air Canada and Canadian Airlines staff to work side by side. Rather than wait for third parties to merge labour groups, a process that may not be complete for some time, we gained union approval for the interim step of intermingling employees by raising the salaries of Canadian employees to Air Canada rates and paying signing bonuses to Air Canada staff. Intermingling, which began in October with passenger agents and continued in February with groundhandling staff, has produced major improvements in productivity and customer service.

There is no denying this merger has been one of the most challenging ever undertaken in this industry given the size and degree of overlap of the carriers. Looking back now, with the merger essentially complete, it is remarkable what we have accomplished in less than one year. The list includes:

- ✓ restructuring Canadian's $3.5 billion debt load and aircraft rent payment obligations, achieving savings of approximately $500 million on a present value basis
- ✓ combining schedules, operating authorities, passenger and cargo terminal operations, system control centres, computer systems, accounting, head offices and frequent flyer programs
- ✓ negotiating long term labour agreements with all but one of our unions
- ✓ training thousands of Canadian employees on Air Canada systems
- ✓ removing redundant domestic capacity and redeploying those aircraft to the transborder network

- ✓ adding overseas destinations, including Sydney and Shanghai
- ✓ ordering 32 aircraft for either growth or fleet renewal
- ✓ establishing one set of commercial policies and practices
- ✓ producing standardized procedures and manuals for the merged carrier
- ✓ creating a single country-wide regional airline system
- ✓ converting Aeroplan and Technical Operations into profit centres to enhance their income generating capacity
- ✓ securing preferred access to Toronto airport's new mega-terminal opening in 2003.

We did this while carrying up to 100,000 passengers a day and we kept our promises to the public by:

- ✓ refraining from involuntary layoffs or relocations of Air Canada or Canadian Airlines staff employed at the time of the acquisition
- ✓ continuing to offer seat sales and other discount fares, and
- ✓ maintaining air service to all Canadian communities served at the time of the acquisition.

And, unlike most of our domestic competitors, we did not raise domestic fares or apply a fuel surcharge in Canada last year.

Already, a number of conclusions can be drawn about the merger. Sixteen thousand jobs were saved. Our acquisition of Canadian averted scenes of stranded travellers, cancelled hockey tournaments and empty resort hotels. The merger created a global powerhouse airline opening up new nonstop routes from Canada to the world. It has opened the way to a new domestic competitive environment in which consumers have more choices in fares and products. Air Canada's Regional Fare Initiative, Websaver fares, year-round Econo-fare discounts and ACFlex fares – discounted business fares with no minimum stay requirement – are making domestic travel more affordable.

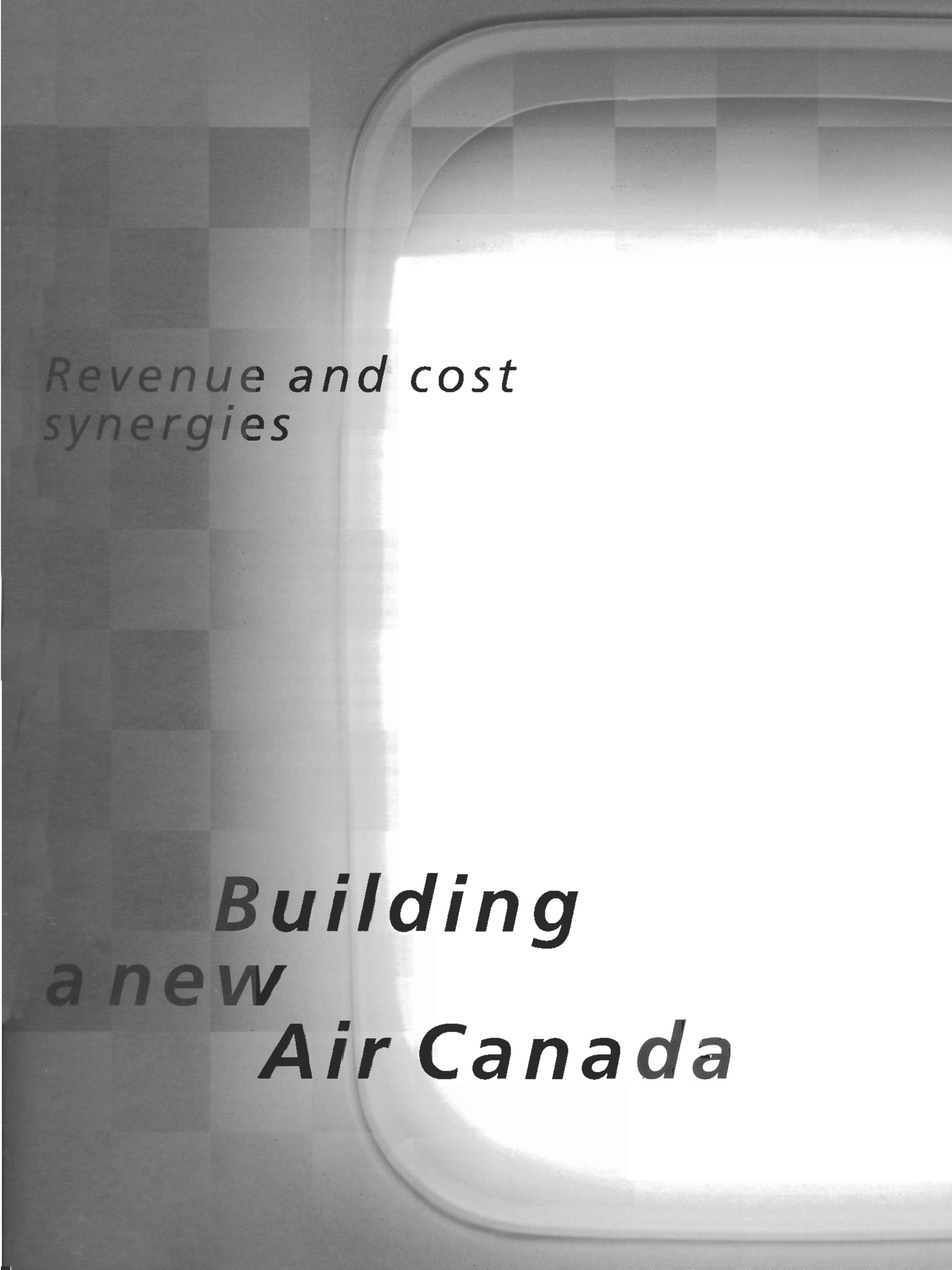
Now we're about to unlock more of the opportunities created by the merger to create new sources of shareholder value, like repositioning Aeroplan with its six million members as a leading loyalty management program capable of significant profit growth. I suspect that when the five-year report card is written, the conclusion will be that the merger and subsequent industry restructuring have produced more durable value for all industry stakeholders – including Air Canada shareholders – than many Canadians expected when this merger odyssey began.

Robert A. Milton
President and Chief Executive Officer

Greater critical mass

Worldwide network

*New routes
and services*



Revenue and cost synergies

Building a new Air Canada

Building a new Air Canada

Merging two large airlines involves a lot of trail blazing. There was no obvious historical template for combining Air Canada and Canadian Airlines. The varied and checkered history of North American airline mergers includes cases where one carrier has been free to cherry pick the key assets of another and cast aside the rest. Other cases have involved merging networks with very little overlap. Neither of these models was applicable here. There was considerable overlap between Air Canada and Canadian, but that duplication represents opportunity for some value creating synergies. Our strategy is to exploit those synergies, creating a new Air Canada, which is greater than the sum of the two airlines. These synergies include the chance to

- build the ideal domestic schedule for business travellers by pooling frequencies and re-spacing frequencies on high density routes
- redeploy redundant domestic capacity to the transborder (Canada-US) market with no significant loss of domestic revenues
- combine virtually all of Canada's primary international route authorities, hitherto split between Air Canada and Canadian, into a powerful global network
- attract more international connections between the Americas and other continents by strengthening our hubs
- generate substantial additional income by merging frequent flyer programs and re-launching Aeroplan as a broader loyalty management program
- use our skilled resources and increased infrastructure to establish a profit centre that expands the amount of contract maintenance work performed for other airlines and
- lower costs by exploiting significantly larger economies of scale.

From the civic standpoint, Air Canada's acquisition of Canadian was preferential to the latter going out of business. The collapse of Canadian would have had ripple effects throughout the economy. Communities would have suffered a reduction or complete loss of air service, over 16,000 employees would have been out of work and tens of thousands of passengers would have been stranded. While integrating Canadian imposed significant costs on Air Canada, there are significant benefits as well. Canadian's international operations, frequent flyer database, skilled work force and

05 *Air Canada, Canadian launch their first joint seat sales of 2000*

04 *Air Canada announces take-up of shares of Canadian Airlines*

20 *Air Canada consolidates regional Airlines for operational, scheduling efficiencies*

27 *Canadian voted Best North American Airline by Official Airline Guide*

JANUARY 2000

customer service orientation were attractive incentives for Air Canada to participate in the restructuring of Canadian's debt. While integrating Canadian has been exceptionally challenging, it has permitted Air Canada greater control over its own destiny. We were able to provide employees and customers with continuity. Once the debt restructuring process was complete, we began leveraging the combined assets of both airlines almost immediately instead of spending years building a comparable worldwide network and infrastructure from scratch.

All airline mergers are stressful and generate their share of inconveniences for customers. Ours was no exception. Many large US airline mergers have taken two or more years to complete; it may be many years before the pending US mergers take full effect. In contrast, our merger took less than a year to complete.

January through June, 2000 – early stage consolidation

When Air Canada's share purchase offer for Canadian was taken up in January 2000, Canadian was losing over $2 million a day. It was imperative to reduce the cash drain as quickly as possible, rationalizing overcapacity and capturing the efficiencies of an integrated schedule, staff, fleet and common product. Almost immediately, planning and preliminary implementation got under way so that if and when Canadian's $3.5 billion debt load was restructured (which happened in June), integration work would be well advanced. Pending the outcome of the debt restructuring, it was necessary to reduce Canadian's losses as much as possible without devaluing or selling Canadian's assets. The first step was to align the two carriers as closely as possible through mutual codesharing and sharing of resources and facilities, while preparing for major integration steps. Those interim measures, necessary to prop up Canadian's finances, caused their share of customer service problems. Mutual codesharing – especially with Air Canada and Canadian operating out of different terminals in Toronto until June – had created confusion among passengers. The airlines' computers couldn't interface with each other. By April, travel demand was at its heaviest ever. With the outcome of the debt restructuring unclear, many Canadians played it safe by booking Air Canada, overtaxing our facilities and resources. The result was congestion and delays, which were addressed in part by hiring and training 2,000 additional employees.

03 *Air Canada invests $23 million to upgrade, expand Dorval technical centre*

02 *Air Canada reports 1999 net income of $213 million and a 7.7% operating margin, highest in 27 years*

29 *Air Canada launches new on-line booking product for top tier business travellers*

FEBRUARY 2000

DEBT RESTRUCTURING

Restructuring Canadian's long term debt was a prerequisite for merging the airlines. It took almost five months to complete – from initial negotiations with creditors in February until a final court ruling approving a plan of reorganization in June. The restructuring resulted in about $500 million of present value savings on debt and aircraft rent obligations as well as the termination of detrimental contracts. Secured creditors received 97 cents on the dollar, unsecured creditors 14 cents.

When airline mergers involve little network overlap, the *modus operandi* is relatively straightforward. Head offices are merged, surplus staff is laid off, everybody who remains dons the same uniform and the business continues under one brand. However, Air Canada and Canadian duplicated each other from coast to coast and in some international markets. That meant merging terminal operations, city ticket offices, call centres, cargo warehouses and much more. Air Canada and Canadian managers set up over 40 joint implementation teams to integrate administration, accounting, ticketing, maintenance operations, IT systems, inflight products, and system control centres. In 10 weeks, a unified summer schedule had been drawn up including 25 new routes. In Toronto, the two airlines were brought into the same facilities. The solution, accomplished with the help of the Greater Toronto Airports Authority, was a daring piece of logistics: To shift other airlines from Terminal 1 to Terminal 3 and to locate all Air Canada and Canadian intercontinental flights at Terminal 1, freeing space in Air Canada's Terminal 2 for Canadian's North American flights. The aging Terminal 1, connected to Terminal 2 by a pedestrian tunnel, was refurbished on the fly. Forty-five related construction projects were completed on budget and on time. On June 2, Canadian employees went to work at Terminal 3, and the next day reported to either Terminal 2 or Terminal 1.

As planning for the terminal shift was under way, other teams focussed on reducing the losses at Canadian by capturing some easy cost savings – the low hanging fruit – from combining operations. Redundant flying was slashed. Canadian's eight aging DC-10-30 widebody jets were removed from the fleet. Tens of millions of dollars were saved through joint advertising, by moving phone and data communications at Canadian to lower Air Canada rates, by streamlining travel agent commission structures between the two airlines and by having Air Canada provide services for Canadian which the latter had been outsourcing. Canadian had been offering volume fare reductions of up to 40 per cent to attract customers. These discounts were reduced when accounts were standardized at Air Canada's corporate rates.

MARCH 2000

09 *Air Canada introduces Express Check-In kiosks to Montreal*

16 *Air Canada, Canadian Airlines extend reciprocal upgrade, mileage redemption privileges for frequent flyers*

21 *Air Canada, Canadian launch spring seat sale*

24 *Canadian Airlines files for bankruptcy protection from creditors*

By June 30, the work had been completed or the contracts negotiated that will secure the bulk of an estimated $700 million in annual net integration synergies by the end of 2001. These synergies fall into three general categories:

- **Redeploying surplus capacity to improve revenue generation.** The former two-carrier system resulted in substantial overcapacity and duplication. Shifting aircraft to new domestic and international routes as well as re-spacing frequencies generated additional revenues.
- **Expanding the international network by capitalizing on new route authorities and feed opportunities.** Due to the limitations of their respective transborder and international networks, Air Canada and Canadian had been handing off a great deal of traffic to alliance partners and non-affiliated airlines at foreign hubs instead of carrying it further. By merging networks and adding foreign destinations as nonstops from Canada, Air Canada has begun carrying that traffic all the way to the final destination.
- **Revenue and cost synergies from leveraging the combined strength of the two airlines.** This represents the largest component of revenue and cost synergies. Major gains are achieved from improved yield management and the discontinuation of distress discounting activities. There are savings from merging airport operations, call centres, ticket offices and head offices and from offering one inflight product. Exploiting greater economies of scale yields savings on everything from aircraft and engine spare parts to phone lines, credit card fees and insurance.

Removing one-time integration expenses and the impact of higher fuel prices, our 2000 operating income would have been $763 million, a $386 million improvement that included the capture of some of these synergies.

DTW YYJ MEX YUL
NRT YEG LAX YYZ

APRIL 2000

03 *Air Canada inaugurates daily Toronto-Tokyo service*

Air Canada, Canadian launch integrated summer schedule including 25 new routes and featuring Air Canada's first services to Mexico City, Tokyo and new Toronto Victoria flight on Canadian.

11 *Air Canada to create up to 170 new accounting jobs in Winnipeg, part of integration plan*

30 *Air Canada's April traffic up 25.3% over April 1999, resulting in a passenger load factor of 75.7%*


Frequent flyer programs
Computer systems

Two cultures

Fleets

Two networks

Merging in quick time

FLEET RENEWAL

A bigger Air Canada provides fleet planners with the opportunity to achieve significant cost and efficiency gains. The expanded customer base enables the airline to employ larger aircraft in certain situations. Now, we can look at using a 50-seat regional jet in place of a 38-seat turboprop, or a 38-seat prop in place of a 21-seater. New sizes of aircraft now have a place in our fleet modeling. A case in point is the 167-seat Airbus A321, an ideal aircraft for high-frequency routes like Toronto-New York and Montreal-Toronto where we need more seats, not more flights. →

July 2000 through February 2001 – the big push

The consolidation of intercontinental flights at Terminal 1 underscores two other benefits of acquiring Canadian: improved fleet efficiency and increased network utility. The merger substantially increases the potential customer base for any route. International traffic which Canadian was carrying or handing off to its former international alliance now provides added support for the enlarged Air Canada network and for future expansion. The bigger the network, the more reason globe-hopping travellers will make Air Canada and our Star Alliance partners their first choice. The merger allowed Air Canada to relaunch services like Toronto-Munich and Vancouver-Shanghai which Canadian or its predecessors had been unable to sustain with a smaller customer base. Combining Air Canada and Canadian's route authorities also meant no longer having to split major markets like Japan and London-Heathrow. While seven US airlines split their country's international passenger routes, Air Canada holds Canada's primary rights to virtually every major overseas market. Only two of those seven US passenger carriers serve China with their own aircraft, and only four have nonstop Tokyo access from their principal hubs. Air Canada has daily nonstop service to Shanghai and Beijing and to three Japanese cities, including Tokyo from both Toronto and Vancouver. Only two US airlines have any Heathrow access; Air Canada serves Heathrow from eight Canadian cities.

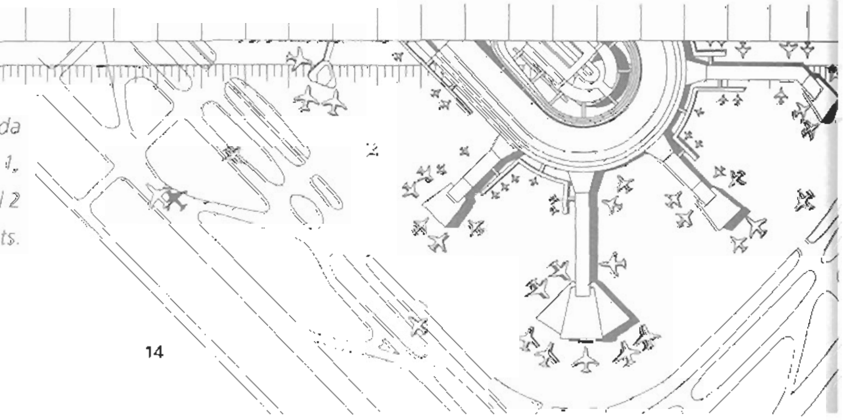
The Toronto consolidation created a hub that can compete with the largest US hubs. This denser Toronto-based network is ideal for capturing more connecting traffic between the Americas and Europe or Asia. Now we can link Zurich or Osaka with Mexico City or São Paulo via Toronto and our other gateways, including Montreal, Calgary and Vancouver. The new mega-terminal in Toronto that will replace Terminal 1 in 2003 and ultimately Terminal 2 is being designed to take maximum advantage of new US customs and immigration preclearance intransit facilities for overseas passengers connecting to US flights. The combined network also makes our cargo appeal stronger. Air Canada Cargo always had a much larger US customer base than did Canadian, and our large US freight forwarder accounts have become strong supporters of Canadian's former Pacific routes now part of the expanded Air Canada network.

26 *Canadian's creditors vote overwhelmingly to accept debt restructuring plan*

10 *Air Canada to appoint ombudsman, create Customer Bill of Rights*

25 *Air Canada and Canadian add capacity to meet soaring domestic demand*

MAY 2000



A daring piece of logistics: locate all Air Canada and Canadian intercontinental flights at Terminal 1, freeing space in Air Canada's Terminal 2 for Canadian's domestic and transborder flights.

After the June 3 terminal switch, merging the airlines required six more major steps, each a project within a project.

PROJECT Move all customers to Air Canada tickets and cargo airwaybills. Done in the fall, this streamlined accounting by creating a single commercial accounting channel for passengers and cargo. This was particularly important for cargo, because customers no longer had to tender freight separately to Air Canada and Canadian terminals, but could tender it all to Air Canada.

PROJECT Combine the two carriers' computer functions. This was in fact a mega-project. Several million lines of software code were rewritten, requiring over 100,000 person/days of labour over a nine-month period, more than double the effort that went into making Air Canada Y2K ready. And it was done in half the time. Both airlines had their own software for almost 300 functions, from inventory management, flight scheduling, baggage handling to airport check-in. The computers had to "speak" to each other before the airline could offer seamless service. Canadian's reservations system was migrated to Air Canada's in October. For the first time, staff at both carriers were able to provide information about any flight in the integrated schedule.

PROJECT Merge employee groups. The first step was to intermingle workers on the ground, so that Air Canada employees could handle Canadian's passengers and flights, and vice-versa. Passenger agents began intermingling in October, and ramp, baggage and cargo staff were intermingled on February 1, 2001. Merging bargaining units, contracts, seniority lists and sorting out union representation questions is expected to be accomplished fairly for all groups through the course of 2001.

→ *where something larger than a 124-seat A320 and smaller than a 191-seat Boeing 767-200 is most advantageous. Twelve A321s will be added to the fleet starting this October, part of orders for 41 new aircraft – A319s, A320s, A321s, A330-300s, 767-300s and in late 2002, the ultra-long-range A340-500. So long as the economy is slowing or even contracting, these deliveries will be offset by selling, subleasing, mothballing or retiring some of the more than 100 older aircraft in the combined fleet.*

YYZ MUC

03 *Air Canada, Canadian complete massive terminal move at Toronto's Pearson Airport*

05 *Air Canada and Star Alliance partner Lufthansa inaugurate daily Toronto-Munich service*

Canadian's 3,500 flight attendants become fourth union to reach agreement on long-term contract

14 *Air Canada, United Airlines introduce industry's first inter-airline electronic ticket*

20 *Air Canada announces trials for in-flight Email, internet services*

27 *Canadian Airlines debt restructuring approved by Alberta court*

JUNE 2000

PROJECT **Merge frequent flyer programs.** Canadian Plus was folded into Aeroplan on schedule on January 1, creating an expanded Aeroplan with six million members – or roughly one in every five Canadians – and a broader base of partner corporations.

PROJECT **Complete the corporate merger of Canadian and Air Canada.** Canadian was folded into Air Canada on January 1, 2001.

PROJECT **Apply for a single Transport Canada Air Operator Certificate (AOC).** One of the final acts of merger, this required extensive planning before the request for a single AOC went to Transport Canada. New manuals, integrated procedures and training had to be prepared so that flight crews, cabin crews and maintenance personnel from both airlines would be operating as one unit, using one set of rules and procedures. Manuals were in employee hands by the end of 2000. The new certificate is expected during 2001.

The merger is essentially complete. There is one Air Canada, one schedule, one airline code, one product, one brand and one administration. Now, work begins on adding new value to the brand. We will be at the forefront in introducing new service features such as Internet and e-mail access on some aircraft that are intended to cement the loyalty of frequent travellers. New aircraft will begin entering the fleet in May.

Our domestic competitors sometimes behave as if they are inventing good service. We beg to differ. In the last few years, Air Canada and Canadian earned some of the most prestigious awards for inflight service and safety that this industry confers. That's a tribute to our management and staff. The merger process has been stressful for them, but we are determined to manage morale issues from the perspective that people need reassurance that their contribution is valued. We plan to provide staff with the training that will help them cope with change, further improve internal communications, improve our awareness of employee needs and concerns. We will also focus on reducing staff surpluses to the greatest degree through attrition, voluntary separation packages and leaves of absence.

02 *Canadian reinstates direct service to Sydney, Australia from Toronto and Vancouver*

05 *Plan announced to merge Canadian Plus and Aeroplan in January 2001*

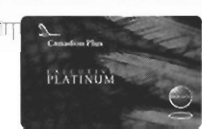
07 *Canadian becomes a wholly owned subsidiary of Air Canada*

12 *Air Canada further enhances medical support on board flights, will equip fleet with portable defibrillators.*

18 *Air Canada says June load factor of 78% highest for that month on record*

24 *Air Canada helps form Aeroxchange, largest airline B2B exchange, to handle US$45 billion in annual industry purchases*

JULY 2000



BETTER DEFENCE AGAINST TOUGH TIMES

The economic slowdown came at an inopportune time given the cost and distractions of merging airlines Yet, the combined operations offer unprecedented flexibility for coping with a downturn. Prior to the merger, Air Canada and Canadian matched each other flight for flight on most major domestic routes. Now, having eliminated that redundancy by re-spacing departures and moving aircraft to other situations, we have a more sustainable domestic schedule and market position for any economic environment. If the domestic economy slows further, we can adjust capacity in ways that don't reduce the overall attractiveness of our product, like reducing frequencies on a route and switching to larger aircraft so we can park more of our older narrowbody aircraft. If the domestic economy is weak but other major economies are strong, we can redeploy domestic aircraft to those stronger Canada-US or international routes. Our merger plan also eliminates much of the surplus created by integration by offering older employees voluntary separation packages. The work force gets younger, and for the next few years unit labour cost growth is lowered by the outflow of employees at the top of the salary scale. There are many opportunities to adjust fleet capacity. A significant number of largely or fully depreciated DC-9s, 737-200s and F28s can be parked at almost no cost. Many more on operating leases can be returned to lessors over the next few years. As part of the restructuring of Canadian's debt, a maturity schedule of leases was established so that the number of older aircraft will contract on an orderly basis. When Canadian's DC-10-30s were retired, some of the lift was replaced by acquiring three Boeing 767-300s on power-by-the-hour leases. We only pay for them when they fly and pay nothing if they sit. Also, some domestic 767-200s are over 18 years old and approaching major scheduled overhauls, making them prime candidates for sale for freighter conversion, an option being actively explored.

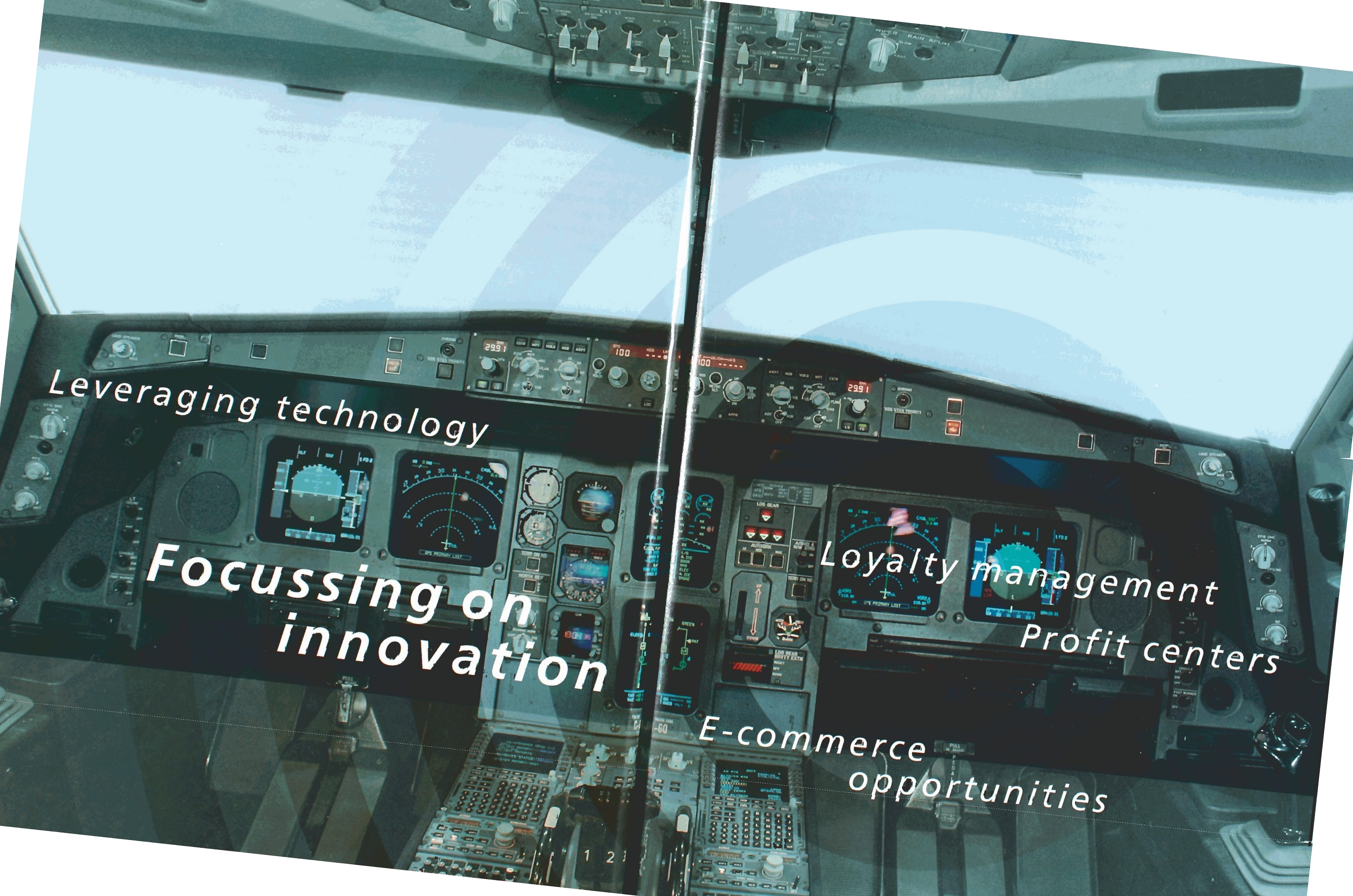
03 *Air Canada unveils 180-day initiative to complete airline services integration; 2,000 hired to improve service*

10 *Air Canada creates new Aeroplan Division to increase Aeroplan contribution to profitability*

30 *Canadian Regional Airlines to join Air Canada network*

31 *United Kingdom competition commission report clears Air Canada-Canadian merger*

AUGUST 2000


Leveraging technology
Focussing on
innovation
Loyalty management
Profit centers
E-commerce
opportunities

February 2001 onward – Unlocking unique merger benefits

With Canadian's traffic added in, Air Canada's domestic market share peaked last summer at all-time highs. Now, the face of competition is a new generation of smaller, rapidly expanding rivals. All are offering discount options. That challenges us to demonstrate how a large unionized airline can be the people's choice and a consistent financial success. Our large asset base has the potential to generate significant additional shareholder value if leveraged aggressively. The goal of our shareholder value enhancement strategy is to achieve greater underlying profitability than the airline could have achieved solely by adding capacity. The strategy has three main thrusts:

- improve airline earnings by raising revenues or lowering unit costs
- find non-airline businesses that attract higher multiples
- convert large expenditures into capital opportunities

Improving airline earnings – Polar routes, express check-in

A large international airline like Air Canada has more opportunities to reduce costs than do smaller operators that begin with low costs and have nowhere to go but... up. One example: Depending on schedule, using new over-the-Pole routings to Asia could generate over $20 million a year in cost savings and revenue enhancements for Air Canada. A second example: Coping with millions of passengers led to development of our Express Check-in Kiosk, winner of the top award in the 2000 Canadian Information Productivity Awards. With the merger, we are putting more kiosks into major airports. Customers love them. With the touch-screen simplicity of the kiosk, check-in takes less than a minute and kiosks also process upgrades and allow a passenger to list himself or herself for an earlier or later flight. Close to 30 per cent of passengers check in by Kiosk where they are available, and the goal is to raise that to 50 per cent in the near term. By the end of last year, 118 kiosks were installed in Canada. And passengers can look forward to other timesaving features like wireless check-in from their cell phones and other handheld devices.

Improving airline earnings – Star Alliance

One of the early acts of merger last year was to add Canadian Airlines to the Star Alliance, the world's largest airline alliance. The combined Air Canada-Canadian customer base is supporting new code-shared service via Star hubs like Frankfurt, Chicago and Toronto and new connections

SEPTEMBER 2000

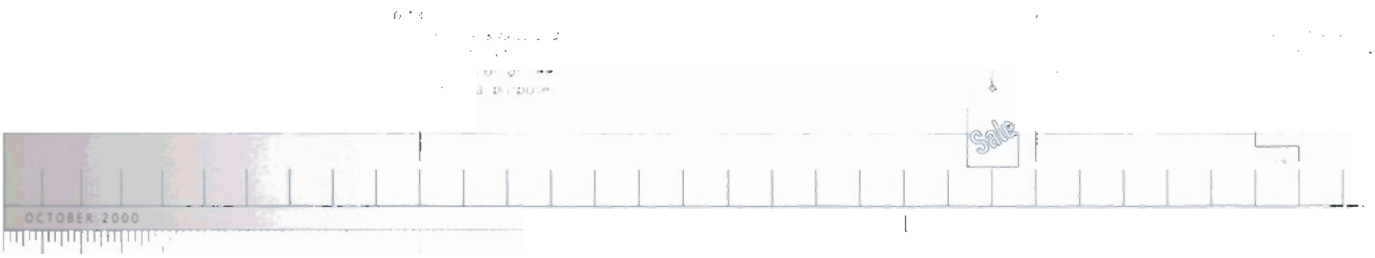
to Southeast Asia over London and Tokyo. That will enable us to compete on a level basis with large US and European airlines which have used their large networks to poach significant Canadian-origin traffic for the Middle East, Asia and Africa. With Star, Air Canada has built a major intra-European hub in Frankfurt that reaches to Moscow, the Baltic states, Eastern Europe and the southern Mediterranean. The expanded Air Canada network also creates new routings within the alliance that attract more high yield traffic onto our flights. Star Alliance also is helping lower costs; member airlines are sharing in approximately US$100 million of annual savings achieved through joint purchasing, sharing of facilities and provision of maintenance and ground handling services.

Improving airline earnings – discount airline

The Canadian public is supporting discount air travel options. Discount carriers are a fact of life, as well as our major competition. Their intention, if not their stated goal, is to take away our customers, our profits, and our jobs. We can do nothing and suffer those losses (which we won't) or participate in the discount sector in some fashion to develop offsetting income. Air Canada's plan is to participate in or collaborate with an airline venture featuring all economy seating with no-frills service. Air Canada only would own the venture if it has competitive costs and the cooperation of our unions.

Non-airline businesses that attract higher multiples – Technical Operations

With five maintenance bases – Montreal, Toronto, Winnipeg, Calgary and Vancouver – Air Canada Tech Ops has first class facilities that would cost over $1.5 billion if built and equipped from scratch. We believe that the potential of this asset is not being reflected in Air Canada's share price. Converting Tech Ops into a business unit whose mandate includes performing more profitable maintenance work for other airlines is a step towards rectifying that. Air Canada has an international reputation for excellence in aircraft maintenance. Until now, third party work has been a sideline for Tech Ops. Work tended to be slotted in around Air Canada maintenance. The new business unit will make third party work a year-round growth activity by focussing on securing long-term contracts that can sustain dedicated maintenance lines. By 2005, it is expected that 40 per cent of the world's commercial carriers will be spending over US$47 billion a year on outsourcing heavy maintenance. This business generates healthy margins 12 months a year, through good economic times and bad. Tech Ops has a skilled work force with extensive knowledge of many airframe models and engine types. Right now, 20 per cent of Air Canada's maintenance work is for other airlines. The goal is to raise that to as much as 50 per cent by the middle of this decade through a combination of new contracts, increased specialization at each base, and the removal of labour intensive older aircraft from the Air Canada fleet.



Non-airline businesses that attract higher multiples – Aeroplan

It's our strategy to convert Aeroplan into a solid loyalty management business. We intend to enable members to earn and redeem points on more non-travel spending and to earn bonus points for on-line browsing and shopping. This is a unique opportunity for Air Canada that comes with merging the country's two major frequent flyer programs; the US has no such leading national loyalty program. First, Aeroplan is adding so-called bricks and mortar partners – such as Future Shop – that purchase and award Aeroplan miles for in-store shopping. The first feature of the online web-hopping and web-shopping expansion will be powered by the Advantex SmartBar™ browser extension, which automatically records points earned for online activity. Advantex Marketing, a TSE-listed company, will manage this program. In exchange, Air Canada has been granted share-purchase rights for up to 35 per cent of Advantex equity on a fully diluted basis, based partly on Aeroplan's revenue contribution. Aeroplan is also investigating options for a broader e-retail mall, part of a dedicated Aeroplan.com website. Aeroplan has been a significant income generator for Air Canada, a fact we feel is not adequately reflected in our share price. Now, it's a profit centre with its own business plan and profit contribution target. Its management also has a mandate to investigate options like converting Aeroplan into a subsidiary and selling a minority stake through an IPO. The increasing presence of Aeroplan on the Internet is indicative of the growing importance of the Net in the airline's sales, marketing and customer service functions.

The Internet is a marvelous vehicle for providing customers with more real-time information. The Air Canada website at www.aircanada.ca has undergone extensive revamping to make it a faster booking engine and provide more real-time information about flight arrival and departure status and Aeroplan mileage balances. There also is huge potential in using the Internet to help automate the airline's supply and distribution chain.

Leverage spending – Technology strategies

When Air Canada chooses a new Information Technology supplier this year, it will be tendering a five to seven year contract worth upwards of $1.5 billion. For that much spending, we are looking for something more than a traditional vendor-customer relationship. We will be exploring other fitting relationships, possibly in the form of a joint venture or partnership interest. Even the very largest airlines are leveraging their purchasing power by entering into consortia or partnerships. Almost three years ago, Air Canada and Star Alliance partners Deutsche Lufthansa AG and UAL Corp, parent of United Airlines, formed AirLiance Materials, a Chicago-based venture to acquire

10 *Air Canada Technical Services formed to develop maintenance operations into a profit centre for third party work*

13 *Check-In Kiosks win top customer service prize: 'Best of Show Award' at Canadian Information Productivity Awards*

21 PVG YVR *Air Canada inaugurates daily Vancouver-Shanghai flights, second destination in China*

29 *For eighth year Air Canada named best business class [illegible] Canada by Business Traveller International*

NOVEMBER 2000

and re-market airline spare parts. AirLiance has helped its owner airlines liquidate large parts inventories as the industry expands just-in-time sourcing. AirLiance's state-of-the-art warehouse and IT system has made it a leading player in the parts marketing sector, and it is now expanding into related parts sourcing activities, like preparing kits of expendable materials for airline maintenance programs. AirLiance is reducing Air Canada's material costs by up to $3 million annually. AirLiance is profitable and looking for significant revenue and income growth this year. Air Canada has a 19.5 per cent equity stake.

Business-to-business e-commerce, or B2B, is destined to be the most important business productivity tool in this industry since the advent of main frame computers. It offers Air Canada the chance to leverage $4 billion of spending on goods other than aircraft, labour and fuel, to lower unit costs and administrative expense. One opportunity is pooling purchasing with other airlines. Another is to automate supply chains – linking our computers with those of preferred suppliers so that they, in effect, manage our procurement needs on a just in time basis, according to pre-determined criteria. Some of our largest suppliers may prefer dedicated computer links. For most, however, the interface will be maintained via Aeroxchange, the world's first B2B exchange for major airlines and suppliers, which Air Canada helped launch last year. With 23 participating airlines representing over 40 per cent of world airline spending, Aeroxchange will help reshape industry procurement practices. It's an investment opportunity for Air Canada, too – we have five per cent of the equity, plus warrants. Automating supply chains will produce labour savings within Air Canada. Suppliers will shave their overhead and better manage their production, making them more cost competitive. Our expectation is that supply chain automation could generate savings for Air Canada in a range of $20-25 million annually.

For Air Canada stakeholders, the application of new technologies and innovative forms of value creation will extract maximum benefits from the synergies and strengths presented by the airline's expanded network and infrastructure. History tells us that advances in technology don't discourage travel. Nor do airline mergers. Quite the contrary, they make travel more convenient while containing or reducing airline costs. Far from making business travel unnecessary, the Internet and wireless communications will liberate people from their cubicles and work spaces to meet their customers and partners and financial backers. The Internet is stimulating our taste for exploring far-off worlds. The expanded Air Canada franchise is built upon a global network ideally suited from the Canadian perspective to accommodate future growth in both inbound and outbound travel. For all Canadians, the world literally unfolds from our hubs and is theirs to conquer.

DECEMBER 2000

Senior Management Team

1 Rupert Duchesne
President – Aeroplan

2 Bill Bredt
Vice President
International

3 Lise Fournel
Executive Vice President
Commercial

4 John M. Baker
Senior Vice President and
General Counsel

5 Ted D'Arcy
Vice President
In-Flight Service

6 Sue Welscheid
Vice President, People

7 Alice Keung
Vice President
Information Technology and
Chief Information Officer

8 Norbert Manger
Vice President, Airports

9 Paul Letourneau
Vice President and
Corporate Secretary

10 Marc Rosenberg
Vice President
Sales and Product
Distribution

11 Michael Downey
Vice President
Flight Operations

12 Robin Wohnsigl
President
Air Canada
Technical Services

13 Ron Clark
Vice President
Corporate Safety and
Environment

14 Paul E. Brotto
Executive Vice President
Planning & Cost
Management

15 Calin Rovinescu
Executive Vice President,
Corporate Development
and Strategy

16 Robert A. Milton
President and Chief
Executive Officer

17 Claude Morin
Vice President, Cargo

18 Rob Giguere
Executive Vice President,
Operations

19 M. Rob Peterson
Executive Vice President and
Chief Financial Officer

20 Rob Reid
Vice President, System
Operations Control

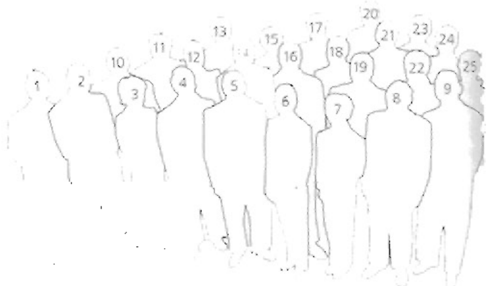
21 Doug D. Port
Senior Vice President,
Customer Service

22 Steve Markey
Vice President
Government Relations &
Regulatory Affairs

23 Paul R. Garratt
Vice President
Financial Planning and
Controller

24 G. Ross MacCormack
Vice President
Alliances and
International Affairs

25 Danielle Poudrette
Vice President
Marketing



Explanatory Notes

Canadian Airlines

Canadian Airlines financial results are included in the Air Canada accounts beginning with the third quarter of 2000. The financial statements, charts and discussion (except where noted) compare Air Canada 2000 results (including Canadian Airlines results for the third and fourth quarters) to Air Canada 1999 results (without Canadian Airlines). For a comparison of the combined operations of the two airlines for the full years 1999 and 2000, refer to pages 36 to 38.

Accounting Policy Changes

During 2000, the Corporation adopted accounting policy changes related to the recognition of third party revenues from frequent flyer programs, Employee Future Benefits and Future Income Taxes. Prior periods have been restated for these changes, except for the policy change related to Future Income Taxes. The restatements of income and retained earnings (deficit) are non-cash in nature and do not affect cash flows from operations. Please refer to note 18 to the consolidated financial statements.

Non-recurring Items

In order to provide a more meaningful comparison of year-over-year results, a number of the following charts, tables and discussions adjust 2000 and prior years for major non-recurring items. These are defined as unusual or special items which are of a one-time nature and do not necessarily reflect the underlying business operation or fundamentals. Non-recurring items include gains on asset sales, one-time integration and labour related charges, the estimated impact of labour disruptions, provisions on the value of retired aircraft and other one-time items as described on page 36 – "Adjusting 1997-2000 Results for Non-recurring Items".

Mainline Operations

The charts, discussion and analysis of results contain references to "mainline operations". This represents airline operations of Air Canada and Canadian Airlines International Ltd. and excludes the operations of Regional Airlines and non-airline subsidiaries.

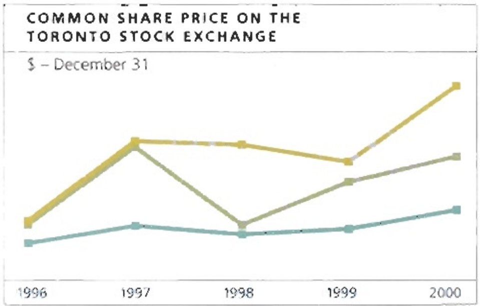
Regional Airlines

Regional Airlines refers to wholly-owned airlines operating under the names of AirBC, Air Ontario, Air Alliance, Air Nova and Canadian Regional.

Air Canada Performance at a Glance

SHAREHOLDER VALUE

COMMON SHARE PRICE ON THE TORONTO STOCK EXCHANGE

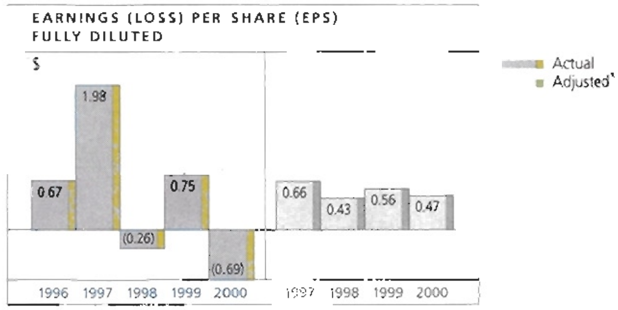


1996	1997	1998	1999	2000	
6.60	15.40	15.00	13.10	21.50	High
6.20	14.75	6.15	10.90	13.70	Close
4.11	6.05	5.10	5.70	7.80	Low

- Common share price rose in 2000 to close at $13.70, up $2.80 from 1999.
- Class A non-voting common shares closed at $11.45, up $1.35 from 1999.
- In December 1999, 68.75 million or 36 per cent of outstanding common and Class A non-voting common shares were bought back and cancelled by way of an issuer bid

EARNINGS

EARNINGS (LOSS) PER SHARE (EPS) FULLY DILUTED



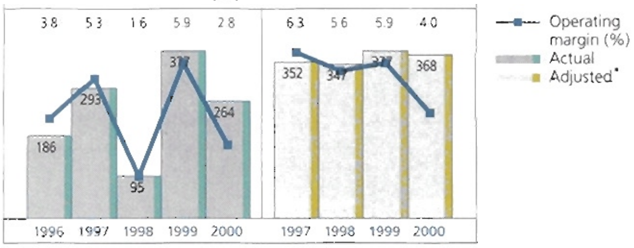
*Adjusted for non-recurring items – See page 36

- Loss per share of $0.69 in 2000.
- Adjusting for non-recurring items, EPS for 2000 of $0.47, fully diluted, as compared to EPS of $0.56, fully diluted, in 1999
- The public commitment not to increase domestic fares constrained Air Canada's ability to compensate for rising fuel prices.
- Higher fuel prices in 2000, relative to 1999, adversely affected 2000 operating income by an estimated $395 million and after-tax earnings by $233 million or $1.55 per share, fully diluted.

More information on page 29.

OPERATING INCOME AND MARGIN

OPERATING INCOME ($M) BEFORE NON-RECURRING LABOUR EXPENSES OPERATING MARGIN (%)

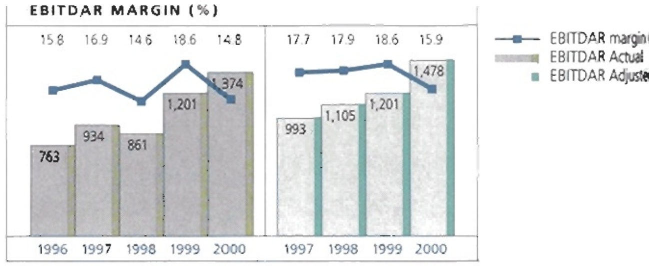


*Adjusted for non-recurring items – See page 36

- Operating income of $264 million, before non-recurring labour expenses, down $113 million from 1999.
- Before non-recurring labour expenses and removing other non-recurring items, operating income of $368 million, down $9 million from 1999.
- Higher fuel prices in 2000, adversely affected operating income by an estimated $395 million compared to 1999 price levels, net of estimated fuel-related fare increases.
- Before non-recurring labour expenses and removing other non-recurring items and the net fuel price impact, operating income would have been $763 million or $386 million above 1999.

EBITDAR

EBITDAR ($M) BEFORE NON-RECURRING LABOUR EXPENSES EBITDAR MARGIN (%)



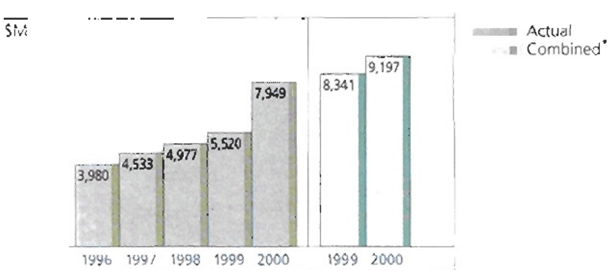
*Adjusted for non-recurring items – See page 36.

- EBITDAR rose $173 million to $1,374 million, before non-recurring labour expenses.
- EBITDAR margin was 14.8 per cent versus 18.6 per cent in 1999.
- Before non-recurring labour expenses and removing other non-recurring items, EBITDAR amounted to $1,478 million, $277 million above 1999. On this basis, EBITDAR margin was 15.9 per cent.

EBITDAR: Earnings (operating income) before interest, taxes, depreciation, amortization and aircraft rent.

PASSENGER REVENUE GROWTH

PASSENGER REVENUES



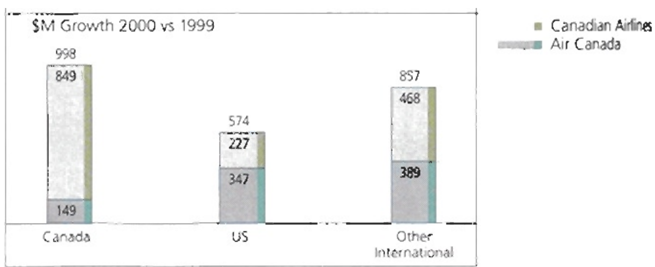
*Air Canada and Canadian Airlines for full year 1999 and 2000 – See page 36.

- In the actual results, Canadian Airlines passenger revenues are included for the July to December 2000 period
- Including Canadian Airlines July-December 2000 results, total passenger revenues grew 44 per cent on a 44 per cent increase in ASM capacity.
- In the combined results, Canadian Airlines published revenues are included for the periods prior to acquisition. On this basis, passenger revenues grew 10 per cent on a 3 per cent increase in ASM capacity.

More information on page 29.

PASSENGER REVENUE GROWTH (cont'd)

PASSENGER REVENUE GROWTH BY SERVICE

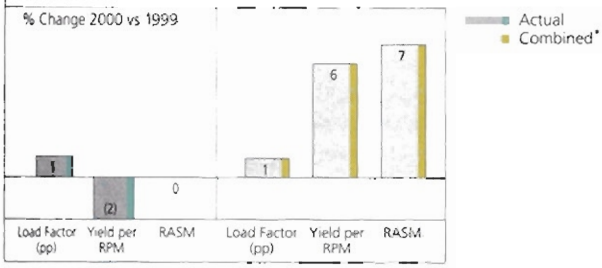


- Significant growth in passenger revenues mainly due to the inclusion of Canadian Airlines revenues from July to December 2000.
- Canada passenger revenue up $998 million or 40 per cent (Canadian Airlines $849 million, Air Canada $149 million or 6 per cent).
- US transborder routes recorded passenger revenue growth of $574 million or 34 per cent (Canadian Airlines $227 million, Air Canada $347 million).
- Other international revenue grew $857 million or 64 per cent (Canadian Airlines $468 million, Air Canada $389 million).

More information on page 29

PASSENGER REVENUE PERFORMANCE

PASSENGER REVENUE PER AVAILABLE SEAT MILE (RASM)



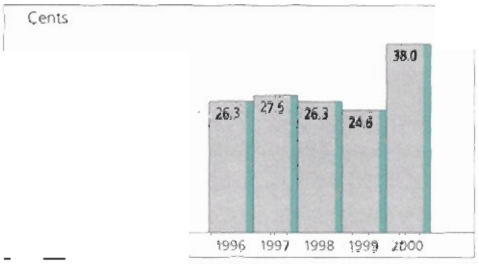
*Air Canada and Canadian Airlines for full year 1999 and 2000 – See page 36.

- With inclusion of Canadian Airlines from July to December 2000, system passenger load factor up 1 percentage point (pp), passenger yield per revenue passenger mile down 2 per cent and RASM for the year unchanged from Air Canada 1999 results.
- On a full year basis, including Canadian Airlines published information for the periods prior to acquisition, RASM rose 7 per cent, on a 6 per cent increase in passenger yield and a 1 percentage point increase in passenger load factor.
- Canadian Airlines RASM has historically been below that of Air Canada.

More information on page 29.

AIRCRAFT FUEL

FUEL PRICE PER LITRE* MAINLINE OPERATIONS



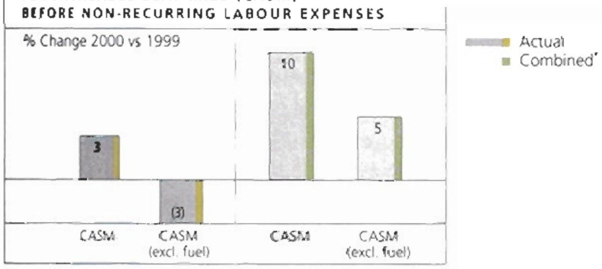
*Net of fuel hedging.

- Aircraft fuel expense rose $749 million or 120 per cent over 1999 on capacity growth of 44 per cent.
- Fuel price per litre, net of hedging, rose 54 per cent.
- Fuel price increase adversely affected operating income by $395 million, net of estimated revenues from fuel-related fare increases in 2000.

More information on page 33

OPERATING COST PERFORMANCE

OPERATING EXPENSE PER AVAILABLE SEAT MILE (CASM) BEFORE NON-RECURRING LABOUR EXPENSES



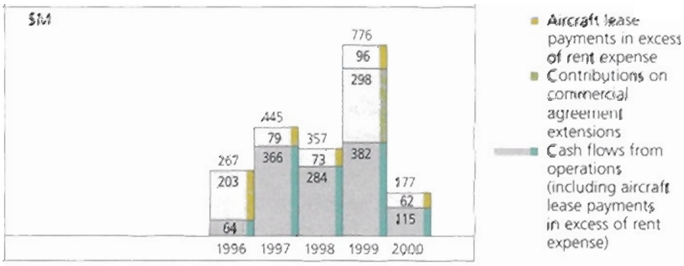
*Air Canada and Canadian Airlines for full year 1999 and 2000 – See page 36.

- Including Canadian Airlines for July to December 2000, CASM for consolidated operations up 3 per cent from 1999, excluding non-recurring labour expenses.
- CASM, excluding fuel expense, down 3 per cent from 1999.
- On a full year basis, including Canadian Airlines published information for periods prior to acquisition, CASM, excluding non-recurring labour expenses, rose 10 per cent.
- On the same basis but excluding fuel expense, CASM rose 5 per cent.

More information on page 32.

CASH FLOWS FROM OPERATIONS

CASH FLOWS FROM OPERATIONS*



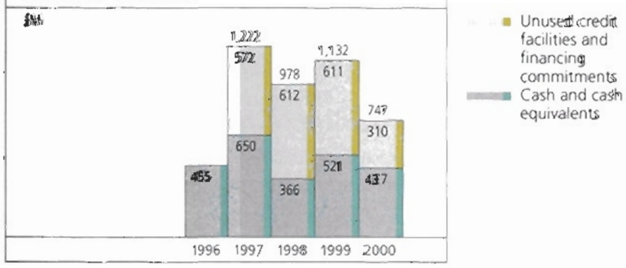
*Excluding aircraft lease payments in excess of aircraft rent expense.

- Excluding aircraft lease payments in excess of aircraft rent expense, cash from operations was $177 million in 2000.
- $298 million of the 1999 cash flows from operations represented cash received for extensions of commercial agreements with Star Alliance and Aeroplan partners.

More information on page 34

LIQUIDITY

CASH, UNUSED CREDIT FACILITIES AND FINANCING COMMITMENTS* AT DECEMBER 31



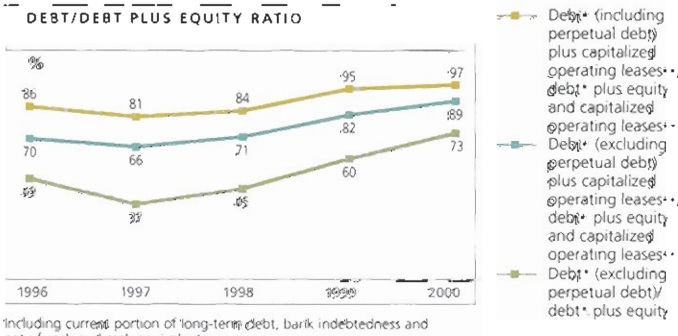
*Excluding financing commitments for aircraft.

- Cash position of $437 million.
- $310 million of unused credit facilities.
- Total cash and unused credit position of $747 million at December 31, 2000.
- Aircraft financing commitments of $2.2 billion at December 31, 2000 are not included.

More information on page 35.

DEBT/DEBT PLUS EQUITY

DEBT/DEBT PLUS EQUITY RATIO



*Including current portion of long-term debt, bank indebtedness and net of cash and cash equivalents.
**Operating leases capitalized at 7.5 times aircraft rent.

- Debt/debt plus equity ratios are up mainly due to a $1,150 million increase in long-term debt and bank indebtedness primarily due to the acquisition of Canadian Airlines.
- Accounting policy changes reduced equity by $329 million in 2000.
- Not included in the equity base are $298 million received in 1999 for extensions of commercial agreements and $182 million invested in long-term leases.
- Perpetual debt viewed by Air Canada as permanent capital.

More information on page 42.

Overview of 2000

On July 6, 2000, following court approval on June 27, 2000 and implementation of Canadian Airlines Corporation's financial restructuring plan, Canadian Airlines International Ltd. (Canadian Airlines) became a wholly-owned subsidiary of the Corporation. As a result of the court approval of the plan of arrangement in late June 2000, the financial position of Canadian Airlines was included in the Corporation's consolidated statement of financial position as at June 30, 2000. The acquisition was accounted for by the purchase method of accounting and assets and liabilities were recorded at their fair values at the time of acquisition.

Canadian Airlines financial results from operations are included in the Air Canada accounts beginning with the third quarter of 2000. The financial statements and this discussion (except where noted) compare Air Canada 2000 results (including Canadian Airlines results for the third and fourth quarters of 2000) to Air Canada 1999 results (without Canadian Airlines). A comparison of the combined operations of the two airlines for the full years 1999 and 2000 can be found on pages 36 to 38.

2000 was a year in which Air Canada embarked upon the most complex corporate restructuring program in Canadian aviation history. Air Canada undertook an operational integration program on an accelerated basis in order to achieve substantial operating revenue and cost benefits. Air Canada had to manage operations with labour agreements which did not allow intermingling of the two airlines' union workforces as well as separate computer reservations and other operating systems. Air Canada put in place revised flight schedules which removed certain inefficient duplication of flying but strong peak summer demand, the different computer reservations systems and labour integration deficiencies led to service weaknesses that required the addition of a significant number of customer service employees. By October 2000, a labour intermingling agreement with customer sales and service agents, together with the move to a single computer reservation system, allowed for improved customer service and more effective labour deployment.

For 2000, Air Canada reported operating income of $86 million, after non-recurring labour expenses, and a net loss of $82 million or $0.69 per share. Removing non-recurring labour expenses and other major non-recurring items, operating income would have amounted to $368 million with a net income of $57 million or $0.47 per share, fully diluted. These earnings included the very significant impact of higher fuel prices, which, net of estimated fuel-related fare increases, adversely affected operating income by $395 million and net income by $233 million or $1.55 per share, fully diluted.

With the acquisition of Canadian Airlines in early July 2000, passenger revenues for the year increased $2,429 million or 44 per cent compared to 1999. Total revenues increased $2,840 million or 44 per cent. Operating expenses rose $2,953 million excluding non-recurring labour expenses of $178 million related to one-time payments principally for the extension of labour contracts and intermingling of certain employee groups. Operating income amounted to $264 million before non-recurring labour expenses as compared to $377 million in the prior year. In addition to the one-time labour expenses, the Corporation's results were also adversely affected by other non-recurring items including an estimated $32 million of lost revenues related to a pilot strike threat and an estimated $72 million of additional costs incurred for the integration of Canadian Airlines. Removing these items and the non-recurring labour expenses ($282 million), operating income would have amounted to $368 million or $9 million below 1999 results.

Escalating fuel prices, the highest in ten years, more than offset the financial synergies of integrating the two carriers in 2000. The public commitment to not increase domestic air fares during the first year of integration significantly constrained Air Canada's ability to compensate for rising fuel prices. Higher jet fuel prices in 2000, as compared to 1999, had an estimated $395 million net unfavourable impact on 2000 operating income ($233 million after tax) based on year 2000 volumes and taking into account estimated passenger revenues from US transborder fuel surcharges and fuel-related international fare increases introduced in 2000. Removing the effect of non-recurring items and the net impact of higher fuel prices, operating income for 2000 would have amounted to $763 million, $386 million higher than 1999.

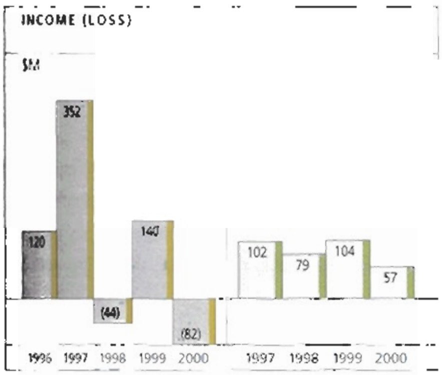
Non-operating expense rose $97 million compared to 1999. Net interest expense increased $56 million mainly as a result of higher debt levels and interest expense from the inclusion of Canadian Airlines. One-time non-operating gains amounted to $35 million ($27 million after tax) reflecting gains from asset sales and purchase of yen perpetual debt partially offset by provisions on the value of retired aircraft and on investments. This compared to non-operating gains of $53 million ($36 million after tax) in 1999 from gains on asset sales, the purchase of yen perpetual debt and aircraft lease restructuring, less one-time costs due to a hostile takeover bid and the write-down of the value of retired aircraft.

Primarily due to the integration of Canadian Airlines, the Corporation incurred significant unusual one-time operating costs in 2000. Adjusting for these and other one-time items noted above ($282 million pre-tax, $166 million after tax) and removing $35 million of one-time non-operating gains ($27 million after tax), net income would have amounted to $57 million or $0.47 per share, fully diluted, in 2000. Adjusting 1999 results for the $36 million of non-operating gains, after tax, Air Canada's 1999 net income would have amounted to $104 million or $0.56 per share, fully diluted.

As at December 31, 2000, the Corporation had $747 million of cash and unused credit facilities.

Earnings

Due to significantly higher fuel costs, non-recurring labour expenses and integration costs, Air Canada recorded a loss of $82 million in 2000 as compared to earnings of $140 million in 1999. Removing non-recurring items in 2000 and 1999, earnings declined $47 million. Increased fuel prices adversely affected 2000 earnings by an estimated $233 million after tax.



*Adjusted for non-recurring items – See page 36.

The following sections (pages 29 to 36) provide year-over-year comparisons for the results as reported in the financial statements. The year 2000 includes 12 months of Air Canada data and six months of Canadian Airlines data whereas the year 1999 reflects 12 months of Air Canada data only. A comparison of the combined operations of the two airlines for 1999 and 2000 can be found on pages 36 to 38.

Operating Revenue Growth

Operating revenues increased $2,840 million or 44 per cent in 2000, with approximately 60 per cent of the increase due to the Canadian Airlines acquisition.

($ millions)	1996	1997	1998	1999	2000
Domestic Routes					
Passenger	1,923	2,031	2,294	2,510	3,508
Cargo	110	116	104	109	146
Total	2,033	2,147	2,398	2,619	3,654
International Routes					
Passenger	2,057	2,502	2,683	3,010	4,441
Cargo	237	271	265	278	396
Total	2,294	2,773	2,948	3,288	4,837
Other Revenue*	513	612	552	536	792
Total Operating Revenues	4,840	5,532	5,898	6,443	9,283
Growth	8%	14%	7%	9%	44%

*Other revenues have been restated due to an accounting policy change related to revenue recognition for loyalty programs (see Note 18 to the Consolidated Financial Statements).

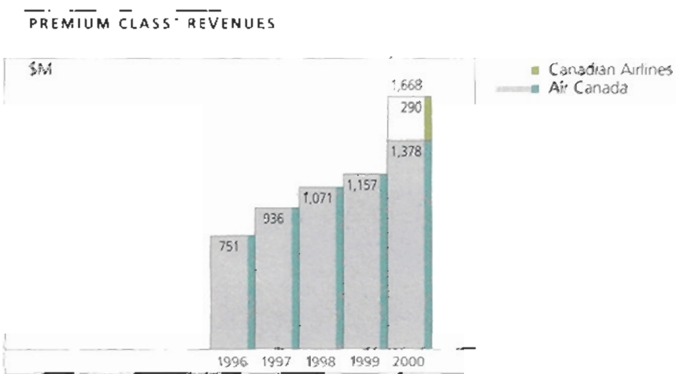
Passenger Revenue Performance

Passenger revenues increased $2,429 million or 44 per cent. Passenger traffic as measured by revenue passenger miles (RPMs) increased 46 per cent on a 44 per cent increase in ASM capacity. Yield per RPM declined 2 per cent and load factor improved 1.1 percentage points. Passenger revenue per ASM (RASM) was unchanged from 1999.

Using combined data for Air Canada and Canadian Airlines for the full year 2000 and 1999, system RPMs increased 4 per cent on a 3 per cent increase to combined ASM capacity. Yield per RPM improved 6 per cent and load factor improved 0.7 percentage points. RASM was 7 per cent higher as compared to combined 1999 results. See page 38.

Premium Class Revenues

Premium Class passenger revenues rose $511 million or 44 per cent in 2000. Canadian Airlines accounted for $290 million of this increase.

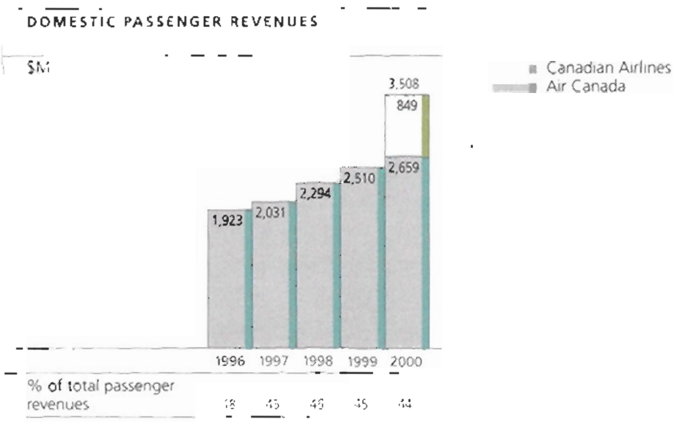


*Including Executive Class and Executive First and, from July to December 2000, Canadian Airlines' Business Class service.

Domestic Passenger Revenues

Domestic passenger revenues experienced growth of $998 million or 40 per cent over 1999 and accounted for approximately 44 per cent of total passenger revenues. The inclusion of Canadian Airlines for the July to December 2000 period accounted for $849 million or 85 per cent of the increase. The greatest revenue growth in Canada was recorded on the Transcontinental routes, linking Toronto, Montréal, Ottawa and Halifax with major western Canada cities including Winnipeg, Calgary, Edmonton and Vancouver. These routes showed a 55 per cent revenue increase and represented 45 per cent of domestic passenger revenues. Revenues for Commuter routes, including Rapidair operations between Toronto and Montréal / Ottawa, grew 22 per cent and accounted for 26 per cent of domestic passenger revenues. Growth on Regional routes, which include operations within eastern and western Canada, amounted to 33 per cent.

Premium revenues on domestic services grew 34 per cent in 2000.

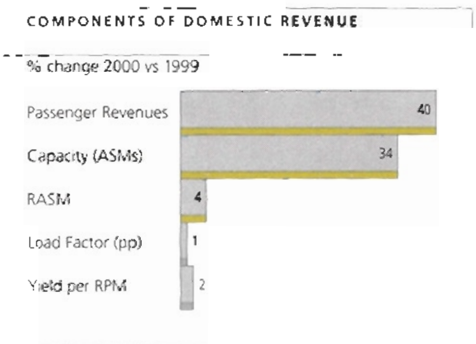


The Importance of RASM

Passenger revenue per available seat mile (RASM) is a common industry measure of passenger revenue performance providing a yardstick of revenue generation per unit of capacity offered. RASM is the product of two key components. The first component is load factor which represents passenger traffic expressed in relation to the capacity offered (i.e. revenue passenger miles (RPMs) to available seat miles (ASMs)). The second component is the yield per revenue passenger mile (or average fare paid per occupied seat mile flown). If an airline can improve its load factor on a particular flight (i.e. the number of revenue passengers) or its yield per revenue passenger mile (i.e. the average fare per mile paid by each passenger) then the passenger revenue per available seat mile (RASM) will increase leading to greater operating profitability on that flight. Depending on market conditions, airlines may periodically have a greater focus on improving load factor or yield, however the interaction of both these factors will determine RASM. The higher the RASM, the more revenue is generated by the airline for each available seat.

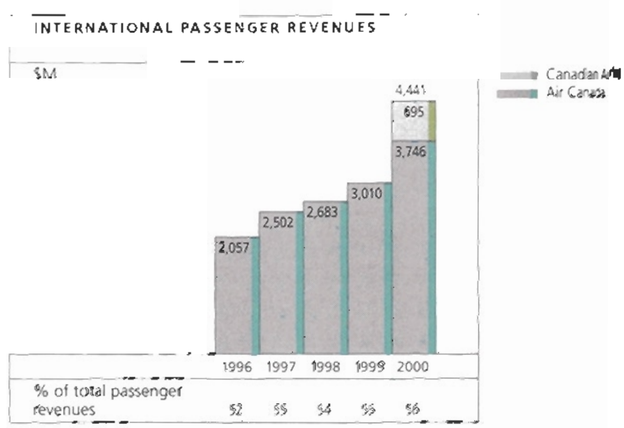
Components of Domestic Revenue

Domestic passenger revenues rose 40 per cent on 34 per cent growth in ASM capacity. Domestic RASM grew by 4 per cent as a result of passenger yield per RPM growth of 2 per cent, partially due to less fare discounting, and a 1 percentage point increase in load factor.



International Passenger Revenues

Passenger revenues from international services, including US transborder services, rose $1,431 million or 48 per cent. Canadian Airlines July to December 2000 revenues accounted for $695 million of the revenue growth.

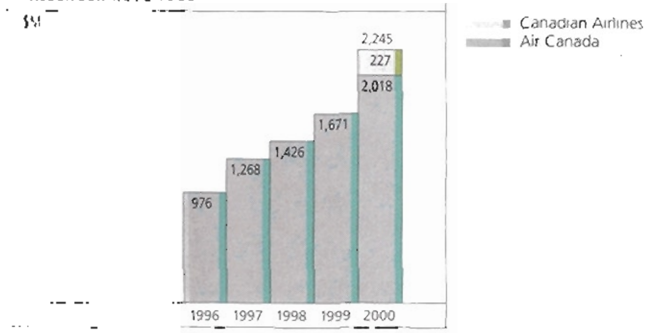


Canada-US Transborder Passenger Revenues

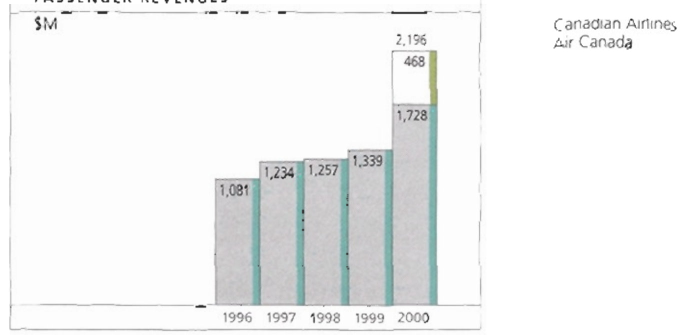
US transborder passenger revenues recorded growth of $574 million or 34 per cent over 1999 and accounted for 28 per cent of total passenger revenues. The inclusion of Canadian Airlines revenues for the July to December 2000 period represented $227 million or 40 per cent of the US transborder revenue growth. US revenues have grown significantly in recent years, as a result of Air Canada's successful expansion of Canada-US services following the introduction of "Open Skies" in February 1995. Air Canada changes in US operations in 2000 included a reallocation of capacity from domestic routes and increased flight frequencies to the key hubs of its US Star Alliance partner, United Airlines.

Executive Class revenues on transborder services grew 39 per cent in 2000.

CANADA-US TRANSBORDER
PASSENGER REVENUES



OTHER INTERNATIONAL
PASSENGER REVENUES



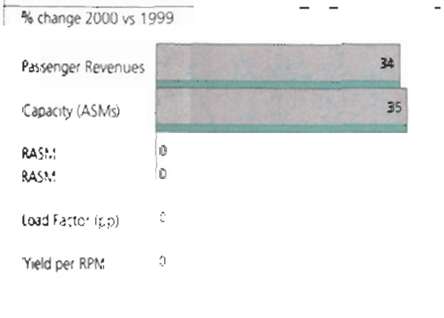
Components of Canada-US Transborder Revenue

US transborder passenger revenues increased 34 per cent on ASM capacity growth of 35 per cent. With virtually unchanged load factor and yield per RPM, the transborder RASM was the same as the 1999 level. Both Air Canada and Canadian Airlines recorded growth in yields and RASM, however the addition of Canadian Airlines' historically lower yielding transborder traffic resulted in a yield and RASM equivalent to Air Canada's 1999 level.

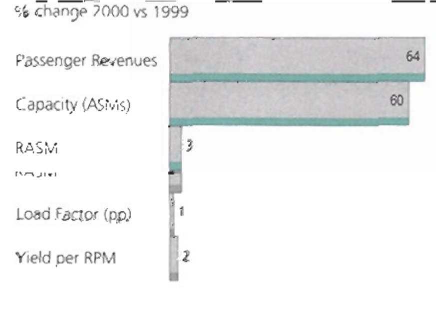
Components of Other International Revenue

Passenger revenues from other international services increased 64 per cent in 2000 on ASM capacity growth of 60 per cent. RASM was up 3 per cent reflecting a 2 per cent increase in yield and a 1 percentage point improvement in load factor. In Atlantic markets, RASM increased 11 per cent due to higher yields and load factors. In Pacific markets RASM grew 4 per cent as a result of better yields. RASM declined for other routes reflecting increased long haul operations, which have lower yields.

COMPONENTS OF CANADA-US
TRANSBORDER REVENUE
% change 2000 vs 1999



COMPONENTS OF OTHER
INTERNATIONAL REVENUE
% change 2000 vs 1999



Other International Passenger Revenues

Passenger revenues from other international routes rose $857 million or 64 per cent in 2000. Of this increase, $468 million represented Canadian Airlines' international route network for the July to December 2000 period. Other international routes made up 28 per cent of total passenger revenues, comprised of Atlantic and Pacific as well as Caribbean and other services. These routes represented approximately 18 per cent, 7 per cent and 3 per cent of total passenger revenues, respectively.

In 2000, Pacific passenger revenues more than tripled, with the inclusion of Canadian Airlines' Asian route network and additional service to Japan and Hong Kong. Atlantic operations recorded a 39 per cent revenue increase, including expansion to Munich, Amsterdam and Milan. Caribbean, South Pacific and Latin America revenues were up 65 per cent over 1999, due largely to Canadian Airlines operations and the start-up of direct services to Sydney, Australia.

Premium revenues on these international services increased 62 per cent in 2000.

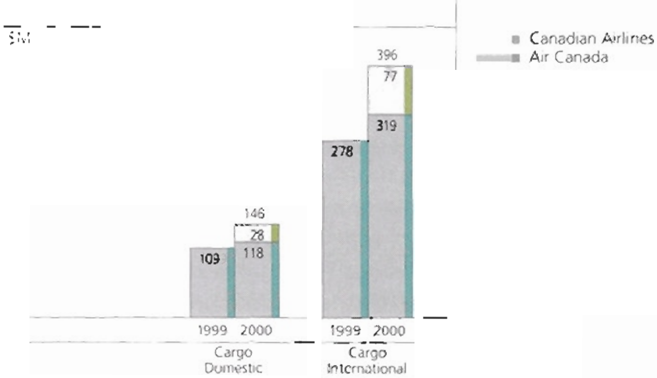
Regional Airlines

Regional Airlines revenues are included in the consolidated revenues. With the inclusion of Canadian Regional revenues for the July to December 2000 period, regional passenger revenues (net of consolidation adjustments) amounted to $1 billion. This represented a $290 million or 41 per cent increase in 2000 on ASM capacity growth of 35 per cent. The acquisition of Canadian Regional accounted for $239 million or 82 per cent of this revenue growth. Domestic revenues rose $237 million or 43 per cent, of which Canadian Regional represented $201 million. US transborder passenger revenues grew $53 million or 35 per cent of which Canadian Regional represented $38 million.

Cargo Revenues

Cargo revenues grew $155 million or 40 per cent in 2000. Domestic routes showed increases of $37 million or 34 per cent while international revenues grew $118 million or 42 per cent respectively. The acquisition of Canadian Airlines accounted for $28 million of the domestic growth and $77 million of the international growth. Air Canada's added capacity on Atlantic and Pacific routes also contributed to the revenue increase.

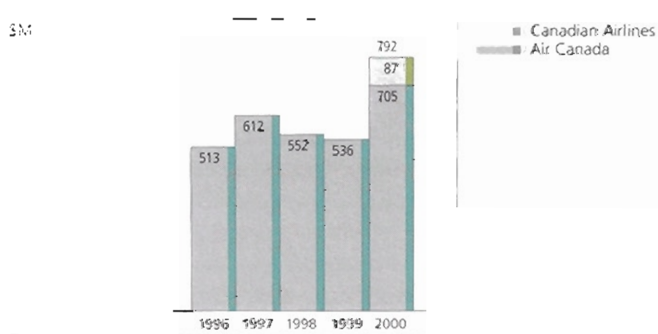
CARGO REVENUES



Other Revenues

Other non-transportation revenues recorded growth of $256 million or 48 per cent. The acquisition of Canadian Airlines contributed $87 million of this increase, net of consolidation adjustments. Frequent flyer revenues have been restated for all periods presented due to an accounting policy change related to revenue recognition of sales of mileage credits to third parties. Following the restatement, Air Canada's frequent flyer revenues were up $83 million as compared to 1999. Other increases pertained mainly to Air Canada Vacations, the sale of surplus aircraft materials and third party maintenance services. Amortization of the 1999 commercial partner contributions for the extension of commercial agreements accounted for $20 million of the increased revenue.

OTHER REVENUES

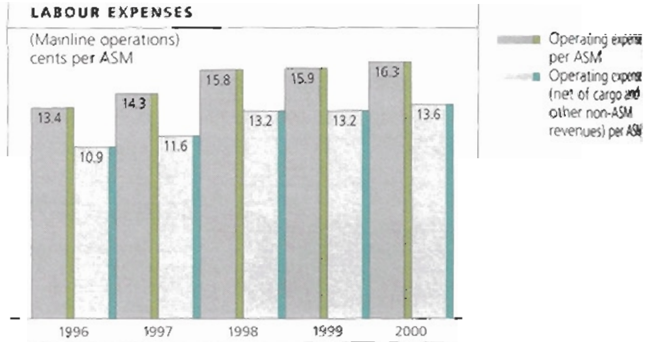


Operating Cost Performance

Operating expense, before non-recurring labour expenses, rose $2,953 million or 49 per cent in 2000 on a 44 per cent increase in ASM capacity.

Mainline unit cost, as measured by operating expense per ASM, excluding Regional Airlines and other non-airline subsidiaries, was 2 per cent above the 1999 level, before non-recurring labour expenses. Significantly higher fuel prices had a major impact on unit costs. Before non-recurring labour expenses and excluding fuel expenses, unit costs declined by 3 per cent from 1999. Operating expense per ASM, net of cargo and other non-ASM revenues, increased 3 per cent to 13.6 cents per ASM, excluding subsidiaries. Canadian Airlines has historically shown lower unit costs than Air Canada. Their inclusion for the July to December 2000 period favourably impacted unit costs. On a combined basis, including Canadian Airlines results for the periods prior to acquisition, unit cost per ASM would have been 10 per cent over 1999 combined levels (5 per cent excluding fuel expenses) reflecting the decreased ASM capacity at Canadian Airlines.

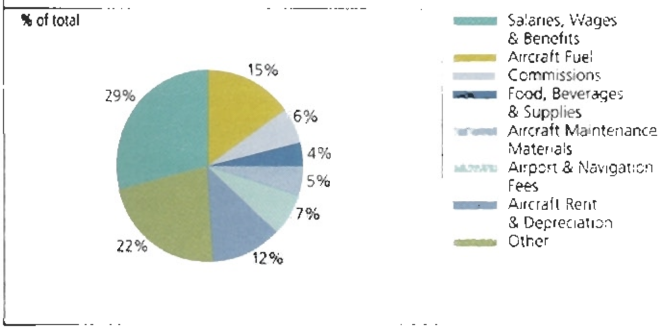
UNIT COST BEFORE NON-RECURRING LABOUR EXPENSES



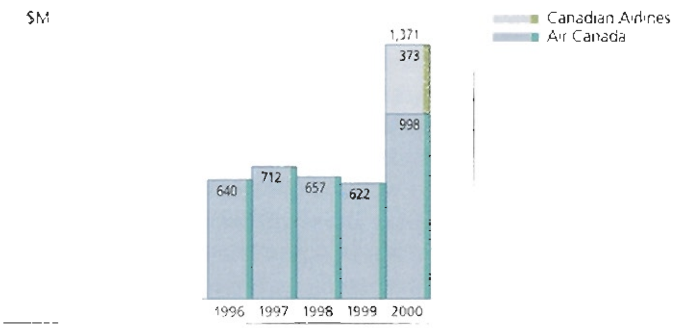
The following describes major cost changes in 2000:

Salaries and wages increased $657 million or 44 per cent on ASM capacity growth of 44 per cent. The salary and wage growth was due mainly to the inclusion of Canadian Airlines for the July to December 2000 period, which represented $426 million or almost two-thirds of the year-over-year increase. Excluding Canadian Airlines, salaries and wages at Air Canada and other subsidiaries rose $231 million or 15 per cent. This increase reflected additional employees hired at Air Canada to resolve customer service issues during the year as well as higher average salaries and greater overtime expense. Prior to October 2000, labour agreements did not permit intermingling of Air Canada and Canadian Airlines sales and service agents and separate computer reservations systems had to be used. As a result, over 2,000 employees were hired to resolve customer service problems caused by these factors, as well as in response to extremely high passenger volumes. Canadian Airlines salaries and wages rose $66 million or 18 per cent in the July to December 2000 period as compared to 1999 Canadian Airlines Corporation results for the same period. In 2000, Canadian Airlines' pilots, flight attendants and sales and service agents signed long-term labour agreements, which included a wage increase to

2000 CONSOLIDATED OPERATING EXPENSES BEFORE NON-RECURRING LABOUR EXPENSES



AIRCRAFT FUEL EXPENSE



Air Canada pay scales. Average salaries at the mainline carriers, including Canadian Airlines in the July to December 2000 period, increased 3 per cent over Air Canada's average salary level in 1999.

Employee benefits expense rose $153 million or 60 per cent. The inclusion of Canadian Airlines for July to December 2000 accounted for $56 million or approximately one-third of this increase. Pension expense at Air Canada rose $65 million over 1999 due mainly to negotiated pension plan amendments and increased employee levels. Group insurance benefits rose $18 million, including post-employment benefits. Mandatory government benefit contributions and other benefits increased $14 million as compared to 1999.

Aircraft fuel was the most significantly increased expense, affecting profitability in 2000, rising $749 million or 120 per cent on a 44 per cent increase in ASM capacity. The inclusion of Canadian Airlines for the July to December 2000 period accounted for $373 million or approximately one-half of this increase. Air Canada's fuel expense, excluding Canadian Airlines, rose $376 million or 60 per cent. The average fuel price per litre, net of hedging, rose 54 per cent over 1999 levels. The difference in jet fuel prices in 2000 as compared to price levels in 1999 had an adverse impact of approximately $395 million on 2000 operating income, based on the year's volumes and net of estimated passenger revenues from transborder fuel surcharges and international fare increases for fuel introduced in 2000. As part of the Canadian Airlines acquisition, Air Canada publicly committed not to increase domestic fares in 2000, which constrained its ability to compensate for rising fuel prices. With the major increase in crude oil prices, fuel hedging had a favourable $79 million impact on 2000 fuel expense, up $62 million from 1999. In 2000, Canadian Airlines did not hedge any of its exposure to fuel prices.

Depreciation, amortization and obsolescence expense increased $94 million or 30 per cent in 2000. Canadian Airlines' inclusion for the period July to December 2000 accounted for $49 million or 52 per cent of this increase. Air Canada's expense, excluding Canadian Airlines, rose $45 million mainly related to information systems and equipment costs and, to a lesser extent, increased depreciation of aircraft.

Commission expense rose $101 million or 24 per cent on passenger and cargo revenue growth of 44 per cent. Commission as a per cent of passenger and cargo revenues declined from 7.1 per cent in 1999 to 6.1 per cent in 2000. This reflected initiatives implemented in 1999 and 2000 to reduce distribution costs including the institution of limits on commissions.

Food, beverages and supplies expense was up $103 million or 39 per cent on a 46 per cent increase to passenger traffic as measured by RPMs. Higher passenger volumes were the main factor for this increase, partially offset by price savings achieved through renegotiation of a major supplier contract.

Aircraft maintenance, materials and supplies expense rose $130 million or 39 per cent. The inclusion of Canadian Airlines results accounted for $94 million or over two-thirds of the increase. Excluding Canadian Airlines, Air Canada's aircraft maintenance expense rose $36 million or 11 per cent over 1999, mainly attributable to increased maintenance on Boeing 767 aircraft as well as higher materials expense including de-icing material costs.

Airport and navigation fees recorded an increase of $165 million or 34 per cent. This reflected capacity growth over the prior year, including the impact of the consolidation of Canadian Airlines for July to December 2000.

Aircraft rent rose $192 million or 37 per cent. The inclusion of Canadian Airlines for the period July to December 2000 accounted for $158 million of the increase. Included in Canadian Airlines' aircraft rent expense were additional Boeing 767 aircraft leased in 2000 to replace DC10 aircraft which were retired in late 1999/early 2000. Air Canada aircraft rent expense rose $34 million, excluding Canadian Airlines, primarily due to additional rent for Airbus A340/A330 aircraft delivered in 1999 and 2000.

The "Other" operating expense category increased $609 million or 45 per cent. Inclusion of Canadian Airlines for the July to December 2000 period accounted for $302 million or approximately one-half of the increase. Air Canada's other expense, excluding Canadian Airlines, rose $307 million or 23 per cent. Air Canada's expenses rose in relation to higher volumes and for costs related to the integration of Canadian Airlines. Increases were recorded in information technology costs, consulting and other fees and training costs as well as for aircraft handling, crew hotels and meals, communications and other expense areas due to increased flying activity and greater passenger volumes. Other subsidiaries, including Regional Airlines, Air Canada Vacations and AirLiance, accounted for $68 million of the expense growth over 1999.

Non-Operating Expense

Non-operating expense totalled $213 million, $97 million above 1999. Net interest expense increased $56 million, mainly as a result of higher debt levels and interest expense from the inclusion of Canadian Airlines. Gains from sale of investments and other assets amounted to $15 million in 2000 as compared to $57 million in 1999. The 2000 gains were comprised of $42 million from asset sales including the sale of landing slots at a US airport, partially offset by $27 million of write-downs on the value of retired aircraft and on investments. The 1999 gains included $67 million from the sale of approximately 60 per cent of the Corporation's interest in Equant NV and $2 million from the sale of another investment and other assets. This was partially offset by expense provisions of $12 million on the estimated sale values of retired aircraft.

Included in other non-operating expense in 2000 were gains of $20 million on the purchase of 5 billion Japanese yen of Air Canada's perpetual debt. In 1999, other non-operating expense included one-time costs of $42 million incurred mainly to defend against a failed hostile takeover bid partially offset by gains of $25 million on the purchase of 6 billion Japanese yen of Air Canada's perpetual debt. In 1999, amortization of deferred foreign exchange included gains of $13 million from the restructuring of eight aircraft leases.

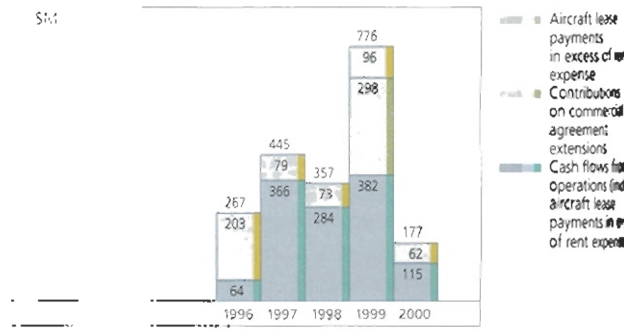
In summary, total non-recurring non-operating gains, net of provisions amounted to $35 million ($27 million after tax) in 2000 while in 1999 non-recurring non-operating gains, net of provisions and expenses, amounted to $53 million ($36 million after tax).

Financial Management

Cash Flows from Operations

2000 cash flows from operations amounted to $115 million as compared to $680 million in 1999. 1999 cash flows from operations included contributions of $298 million from the extension of the Aeroplan frequent flyer commercial agreement with the Canadian Imperial Bank of Commerce and from the extension of commercial agreements with Star Alliance partners, United Airlines and Lufthansa. Aircraft lease payments in excess of aircraft rent expense represent a negotiated outflow of operating cash related to aircraft leases, either at the inception or during the term of a lease when cash payments are in excess of the amounts recorded for aircraft rent expense. These outflows were $62 million in 2000 as compared to $96 million in 1999. Excluding these amounts and the 1999 contributions on commercial agreement extensions, cash from operations in 2000 amounted to $177 million versus $478 million in 1999. The $301 million decline in adjusted cash from operations was mainly related to lower earnings in 2000.

CASH FLOWS FROM OPERATIONS

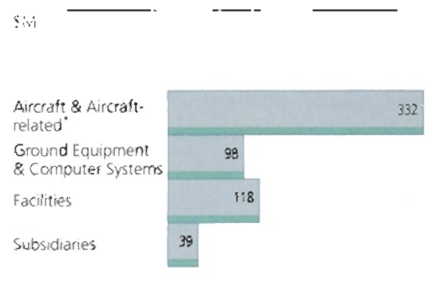


Financing and Investing

During 2000, new borrowings amounted to $761 million and were comprised mainly of a $294 million facility guaranteed by two Star Alliance partners, a $270 million drawing against a credit facility and a net $197 million of bank indebtedness related to a refinancing of Canadian Airlines debt. Repayments of long-term debt totalled $490 million during the year and included a $276 million repayment of Canadian Airlines high yield bonds, as well as mandatory and optional debt repayments by Air Canada and its subsidiaries.

Proceeds from sale and leaseback of assets amounted to $292 million in 2000 due to the leasing of four Airbus A319 aircraft and two A330 aircraft. Sale of investments and other assets provided cash proceeds of $45 million, of which $35 million was from the sale of landing slots at a US airport.

2000 CAPITAL EXPENDITURES



*Net of recovered progress payments

Additions to property and equipment totalled $587 million in 2000. Aircraft and aircraft-related expenditures were $332 million for Air Canada and included progress or final payments on Airbus A330, A340, A321 and A319 aircraft. During the year, two previously leased

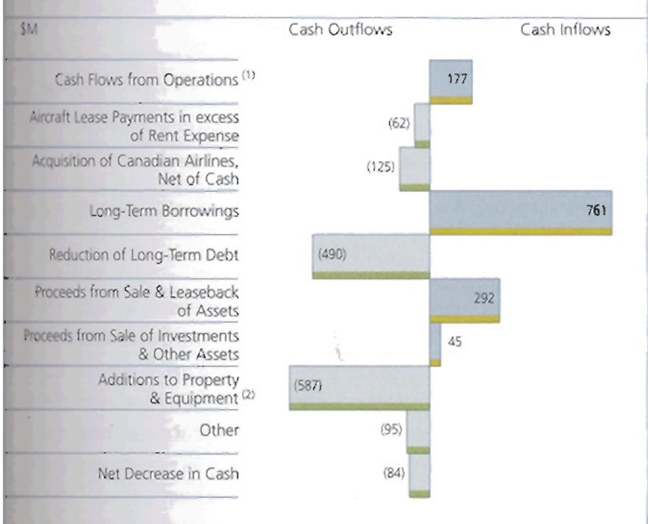
Boeing 767-200s were purchased. Also included were payments for aircraft betterments, spare engines and inventory. Recoveries of progress payments on aircraft amounting to $49 million were netted against additions to aircraft expenditures. This represented the recovery of progress payments made in prior years, upon completion of lease financing of new aircraft. Expenditures for ground and computer equipment and computer systems development amounted to $98 million. Facilities expenditures were $118 million and included expenditures for the development and upgrade of Terminals 1 and 2 and cargo facilities at Toronto's Pearson International Airport. Subsidiary capital expenditures, including Canadian Airlines, were $39 million.

The $131 million Canadian Airlines acquisition (of which $6 million was invested in 1999 and $125 million was invested in 2000) represented the investment in common shares of Canadian Airlines Corporation and preferred shares of Canadian Airlines as well as fees, net of Canadian Airlines' cash balances at the acquisition date.

Investments and advances of $81 million related mainly to an indirect financing provided to Canadian Airlines.

Cash and cash equivalents at December 31, 2000 were $437 million, down $84 million from 1999.

2000 CHANGES IN CASH POSITION



(1) Excluding aircraft lease payments in excess of aircraft rent expense
(2) Net of recovered progress payments

1999 Issuer Bid and Related Funding

In the fourth quarter of 1999, the Corporation completed a $1.1 billion issuer bid by purchasing 68.75 million Air Canada shares at a price of $16.00 per share. A total of 41.67 million common shares and 27.08 million Class A non-voting common shares were purchased and cancelled. During the fourth quarter of 1999, funding arrangements of over $700 million were concluded. Please refer to note 11 to the Consolidated Financial Statements.

Canadian Airlines Corporation Financial Restructuring

During 2000, Canadian Airlines completed a financial restructuring of its debt, lease and other obligations prior to the completion of the acquisition of Canadian Airlines by Air Canada. The restructuring was approved by the courts in late June 2000. As a result of the restructuring, future payment obligations for debt and aircraft leases were reduced by approximately $500 million, measured on a present value basis. As well, as a result of the restructuring and the comprehensive revaluation of Canadian Airlines, its shareholders' deficiency prior to the acquisition was lowered by more than $600 million. As a result of the Canadian Airlines acquisition, the Corporation recorded goodwill of $502 million which is being amortized over a 40 year period.

Liquidity

As at December 31, 2000, the Corporation had cash and unused credit facilities of $747 million with a bank indebtedness and short-term loan position of $264 million. The cash and unused credit facilities were comprised of $437 million of cash and cash equivalents and $310 million of unused credit facilities. Unused credit facilities consisted of a $175 million one-year committed credit facility, other credit lines totalling $100 million and the $35 million unused portion of a US$370 million unsecured revolving credit facility. Air Canada's total availability under credit facilities was $830 million as at December 31, 2000 of which $520 million was drawn. At December 31, 2000, the current portion of long-term debt was $529 million and bank indebtedness and short-term loans were $264 million.

The Corporation completed, in late February 2001, the issuance of $250 million aggregate principal amount of 9 per cent senior unsecured debentures due June 2006. Proceeds will be used for debt refinancing and for general corporate purposes. The Corporation completed a US$68 million sale and leaseback of certain assets in early March 2001. Air Canada also entered into an agreement, in early March 2001, with a group of purchasers for the sale of US$300 million and 100 million Euros aggregate principal amount of 10.25 per cent senior unsecured notes due 2011, on a private placement basis, sold at a discount to yield 10.5 per cent. The closing of this placement is expected to take place by mid-March 2001. Net proceeds of the offering, estimated at US$378 million, will be used to refinance existing debt. The Corporation's target is to achieve a total cash and available credit position of $1.5 billion in 2001.

As at December 31, 2000, Air Canada had additional commitments from financial institutions to provide financing of $2.2 billion for aircraft deliveries in the 2001 to 2003 period. In early February 2001, the Greater Toronto Airports Authority (GTAA) paid Air Canada $130 million relating to the GTAA's December 2000 commitment to acquire certain assets at Toronto's Pearson International Airport.

Adjusting 1997-2000 Results for Non-recurring Items

The tables below adjust 1997 through 2000 results for major non-recurring items. On an adjusted basis, operating income for 2000 was $368 million as compared to $377 million in 1999 and net income was $57 million versus $104 million in 1999.

($ millions except per share amounts)	Actual Results	Pilot Strike/ Strike Threat (Estimated)	Gains and Other One-Time Items	Adjusted Results
2000				
Operating revenues	9,283	32	–	9,315
Operating expenses	9,019	–	(72)[1]	8,947
Operating income before non-recurring labour expenses	264	32	72	368
Non-recurring labour expenses	178	–	(178)	–
Operating income	86	32	250	368
Non-operating expense	(213)	–	(35)[2]	(248)
Income (loss) before income taxes	(127)	32	215	120
Recovery of (provision for) income tax	45	(13)	(95)	(63)
Income (loss) for the year	(82)	19	120	57
Earnings (loss) per share – fully diluted	$ (0.69)	$ 0.13	$ 0.80	$ 0.47
1999				
Operating revenues	6,443	–	–	6,443
Operating expenses	6,066	–	–	6,066
Operating income	377	–	–	377
Non-operating expense	(116)	–	(53)[3]	(169)
Income (loss) before income taxes	261	–	(53)	208
Recovery of (provision for) income tax	(121)	–	17	(104)
Income (loss) for the year	140	–	(36)	104
Earnings (loss) per share – fully diluted	$ 0.75	–	$ (0.19)	$ 0.56

(1) $72 million of estimated integration related operating expenses ($42 million after tax).
(2) Gains on sale of assets $42 million; gains on purchase of Japanese yen perpetual debt $20 million; less provisions on the value of retired aircraft and on investments $27 million; for a total net gain of $35 million ($27 million after tax).
(3) Gains on sale of investments and other assets $69 million; gains on purchase of Japanese yen perpetual debt $25 million; gains from restructuring of aircraft leases $13 million; less one-time costs mainly to defend against a failed hostile takeover bid $42 million; and provisions on the value of retired aircraft $12 million; for a total net gain of $53 million ($36 million after tax).

($ millions except per share amounts)	Actual Results	Pilot Strike/ Strike Threat (Estimated)	Gains and Other One-Time Items	Adjusted Results
1998				
Operating revenues	5,898	263	–	6,161
Operating expenses	5,803	13	(2)[1]	5,814
Operating income	95	250	2	347
Non-operating expense	(173)	–	(30)[2]	(203)
Income (loss) before income taxes	(78)	250	(28)	144
Recovery of (provision for) income tax	34	(95)	(4)	(65)
Income (loss) for the year	(44)	155	(32)	79
Earnings (loss) per share – fully diluted	$ (0.26)	$ 0.81	$ (0.16)	$ 0.43
1997				
Operating revenues	5,532	74	–	5,606
Operating expenses	5,239	17	(2)[3]	5,254
Operating income	293	57	2	352
Non-operating income (expense)	98	–	(236)[4]	(138)
Income (loss) before income taxes	391	57	(234)	214
Provision for income tax	(39)	(25)	(48)[5]	(112)
Income (loss) for the year	352	32	(282)	102
Earnings (loss) per share – fully diluted	$ 1.98	$ 0.17	$ (1.49)	$ 0.66

(1) $2 million fuel excise tax rebate repayment resulting in $10 million of income tax benefits.
(2) Gains on sale of investments and other assets, net of provisions, $30 million ($24 million after tax)
(3) Fuel excise tax rebate repayment of $43 million offset by $41 million mainly related to lower pension expense.
(4) Gains on sale of investments and other assets, net of provisions, $236 million ($169 million after tax).
(5) Including a net $115 million reduction to the tax provision primarily related to the $43 million fuel excise tax rebate repayment

2000 Year-over-year Comparison Including Canadian Airlines Operating Income Results

In order to view 2000 operating results on a more comparable year-over-year basis, the following unaudited financial data compares:

- The sum of 2000 consolidated operating income results of Air Canada (AC) including Canadian Airlines International Ltd. (CAI) from July to December 2000 and publicly available Canadian Airlines Corporation (CAC) results for January to June 2000, excluding special restructuring expenses incurred by CAC, to:
- The sum of Air Canada (AC) 1999 results and the publicly available 1999 consolidated results of Canadian Airlines Corporation (CAC).

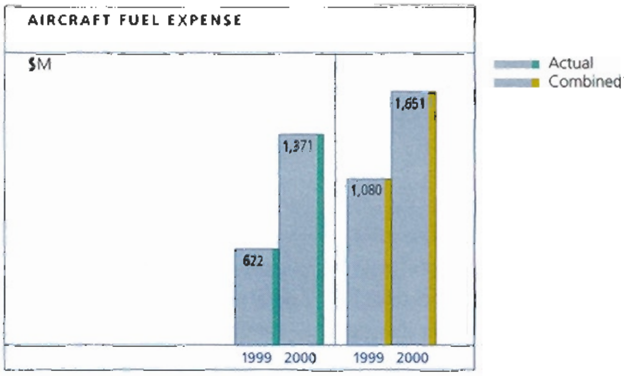
In 1999, Air Canada did not hold any ownership interest in CAC or CAI and no adjustments have been made to published CAC results for 1999 and the first six months of 2000, other than the exclusion of restructuring expenses.

The analysis does not reflect any adjustments that would result from accounting for the acquisition of Canadian Airlines under the purchase method of accounting nor any adjustments to revenues or expenses that may be required had an acquisition date of January 1, 2000 or January 1, 1999 been assumed. The analysis would also not be indicative of what might have occurred, had the acquisition been made on these dates, nor is it indicative of future events.

Using data that combines consolidated financial results for Air Canada and Canadian Airlines, the airlines recorded an operating loss of $101 million in 2000 compared to operating income of $235 million in 1999. Removing non-recurring items estimated at $282 million, combined 2000 operating results would have heen $54 million below the carriers' combined results in the prior year. Non-recurring items included $178 million of non-recurring labour expenses in the form of one-time payments principally for extending collective agreements and to achieve intermingling of certain employee groups. As well, the Corporation incurred an estimated $72 million of additional non-recurring integration and customer service costs and lost an estimated $32 million of operating income due to the impact of a pilot strike threat in mid-year 2000.

Management estimates that synergies of over $300 million from revenue gains and cost reductions were realized in 2000 from the Canadian Airlines acquisition and integration as compared to separate operations in 1999.

The benefits from integration were more than offset by the dramatic increase in the price of fuel. The impact on 2000 fuel expense was an estimated $500 million due to fuel price escalation alone, net of estimated incremental revenues from fuel-related fare increases in 2000. Adjusting 2000 results for non-recurring items and the net fuel price impact, operating income would have amounted to $681 million or $446 million better than the combined 1999 result.



*Air Canada and Canadian Airlines for full year 1999 and 2000.

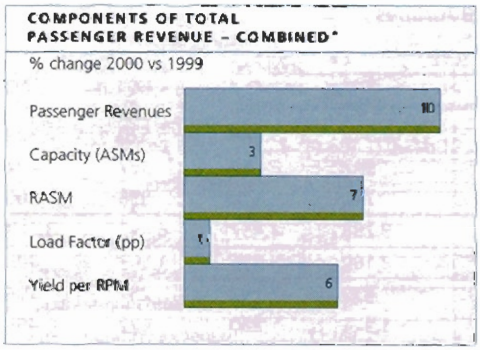
Air Canada and Canadian Airlines – Combined Consolidated Operations including Regional Airlines

(unaudited – millions)

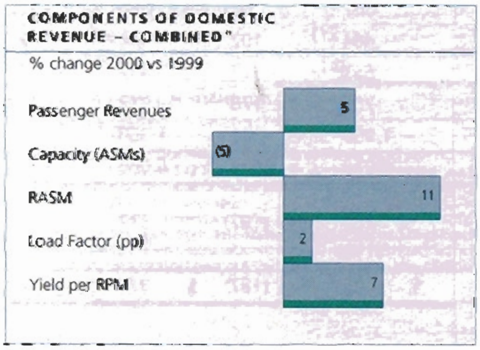
	2000 AC+CAC/CAI	1999 AC+CAC	$ Change	% Change	Published Results 2000 AC/CAI	2000 CAC unaudited Jan-Jun	1999 AC	1999 CAC
Passenger revenue	$ 9,197	$ 8,341	$ 856	10	$ 7,949	$ 1,248	$ 5,520	$ 2,821
Cargo revenue	641	629	12	2	542	99	387	242
Other revenue	902	736	166	23	792	110	536	200
Total operating revenues	10,740	9,706	1,034	11	9,283	1,457	6,443	3,263
Salaries & wages	2,516	2,211	305	14	2,160	356	1,503	708
Benefits	462	361	101	28	410	52	257	104
Aircraft fuel	1,651	1,080	571	53	1,371	280	622	458
Depreciation, amortization & obsolescence	464	450	14	3	405	59	311	139
Commissions	619	676	(57)	(8)	521	98	420	256
Food, beverages & supplies	436	426	10	2	367	69	264	162
Aircraft maintenance, materials & supplies	571	573	(2)	0	464	107	334	239
Airport & navigation fees	774	773	1	0	657	117	492	281
Aircraft rent	883	867	16	2	705	178	513	354
Other	2,287	2,054	233	11	1,959	328	1,350	704
Total operating expenses	10,663	9,471	1,192	13	9,019	1,644	6,066	3,405
Operating income (loss) before non-recurring labour expenses	77	235	(158)		264	(187)	377	(142)
Non-recurring labour expenses	(178)	–	(178)		(178)	–	–	–
Operating income (loss)	(101)	235	(336)		$ 86	$ (187)	$ 377	$ (142)
Add back estimated impact of non-recurring items:								
Pilot strike threat	32	–	32					
Non-recurring labour expenses	178	–	178					
Integration/customer service	72	–	72					
	282	–	282					
Operating income excluding estimated non-recurring items	$ 181	$ 235	$ (54)					

Operating Statistics	2000 AC+CAC/CAI	1999 AC+CAC	% Change	2000 AC/CAI	2000 CAC Jan-Jun	1999 AC	1999 CAC
Revenue passenger miles (RPM) (millions)	**44,968**	43,379	3.6	37,536	7,432	25,623	17,756
Available seat miles (ASM) (millions)	**63,417**	61,778	2.6	52,553	10,864	36,438	25,340
Passenger load factor %	**70.9**	70.2	0.7 PP	71.4	68.4	70.3	70.1
Passenger revenue yield per RPM (cents)	**20.4**	19.2	6.4	21.2	16.8	21.5	15.9
Passenger revenue per ASM (cents)	**14.5**	13.5	7.4	15.1	11.5	15.1	11.1
Operating expense per ASM, excluding non-recurring labour expenses (cents)	**16.8**	15.3	9.7	17.2	15.1	16.6	13.4
Operating expense per ASM, excluding non-recurring labour expenses and fuel expense (cents)	**14.2**	13.6	4.6	14.6	12.6	14.9	11.6

Passenger revenues rose $856 million or 10 per cent on a 3 per cent increase to available seat mile (ASM) capacity compared to the prior year sum of Air Canada and CAC operations. Passenger yield per revenue passenger mile was up 6 per cent and passenger traffic increased 4 per cent. Passenger revenue per available seat mile improved 7 per cent over the combined Air Canada and CAC 1999 results.



*Air Canada and Canadian Airlines for full year 1999 and 2000



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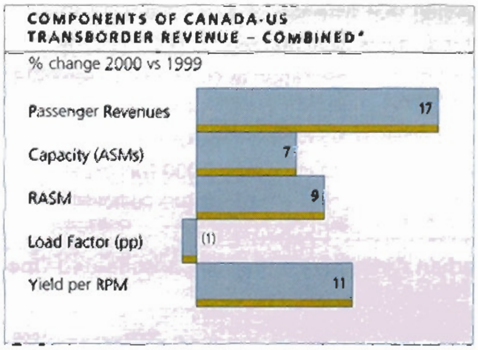
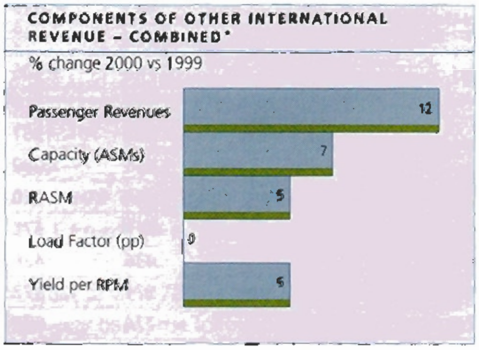


*Air Canada and Canadian Airlines for full year 1999 and 2000



*Air Canada and Canadian Airlines for full year 1999 and 2000

Fuel expense was the most significant expense factor rising $571 million or 53 per cent with only a 3 per cent increase to combined AC and CAC flying capacity. Salaries and wages were up $305 million or 14 per cent due, in part, to additional employees hired to correct customer service issues caused by lack of labour intermingling and incompatible computer reservations systems. Other factors included higher Air Canada average salaries and overtime expenses and increased salaries at Canadian Airlines. Employee benefits expense rose $101 million or 28 per cent mainly as a result of greater pension and other benefit costs due to negotiated pension plan amendments and greater employee levels. Most other expense areas showed limited or no growth except other operating expenses which rose $233 million or 11 per cent. The growth in this category reflected greater flying activity and additional integration costs partially offset by expense reductions in advertising and other expense areas.

Work Force

During 2000, Air Canada had an average of 25,029 employees, measured on a full-time equivalent (FTE) basis as compared to 22,991 employees in 1999, excluding subsidiaries. In 2000, Canadian Airlines had an average of 13,211 FTE employees for the full year, excluding Canadian Regional and non-airline subsidiaries, as compared to 14,036 FTE employees in 1999. The Regional Airlines, including Canadian Regional, and other non-airline subsidiaries of Air Canada and Canadian Airlines had an average of 5,274 FTE employees during 2000 as compared to 5,047 FTE employees in 1999.

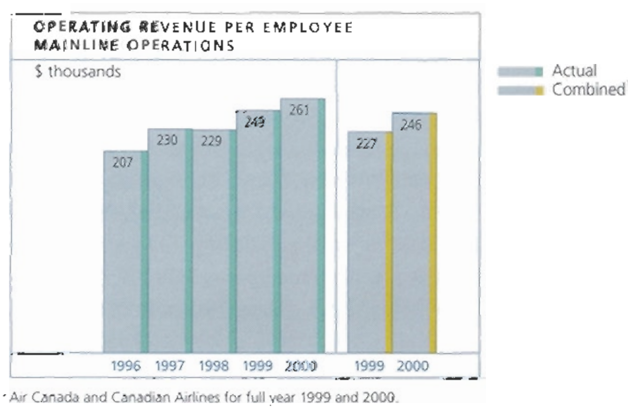
In the fourth quarter of 2000, the Corporation had an average of 45,123 FTE employees as described below:

Employee Group	Union [1]	FTE Employees [2] 4th Qtr 2000	% of Total	FTE Employees [3] 4th Qtr 1999	% of Total	Change
Mainline (AC+CAI)						
Management & administrative support employees	n/a	5,600	12	5,568	13	32
Pilots	ACPA /ALPA	3,086	7	3,031	7	55
Flight attendants	CUPE	7,615	17	6,872	17	743
Customer sales & service agents	CAW/IBT	7,892	18	7,168	17	724
Maintenance, ramp & cargo employees	IAMAW	13,202	29	11,890	29	1,312
Unionized finance/administrative employees	IAMAW	886	2	842	2	44
Other unionized employees	various	1,446	3	1,322	3	124
Total **Mainline**		39,727	88	36,693	88	3,034
Regional Airlines and other subsidiaries	various	5,396	12	5,037	12	359
Consolidated total		45,123	100	41,730	100	3,393

(1) ACPA: Air Canada Pilots' Association; ALPA: Air Line Pilots Association; CUPE: Canadian Union of Public Employees; CAW: Canadian Auto Workers Union; IBT: International Brotherhood of Teamsters; IAMAW: International Association of Machinists and Aerospace Workers.
(2) Fourth quarter 2000 employee counts include 472 FTE employees for the insourcing of work previously done by AMR Corporation and other third parties for Canadian Airlines.
(3) Due to reclassification of employees and revised methodology, FTE employee counts for Canadian are different from employee counts published in 1999 by Canadian Airlines Corporation.

Employee productivity, as measured by operating revenue per employee increased 5 per cent from 1999 for mainline operations, including Canadian Airlines beginning with the third quarter of 2000. The July to December period includes the seasonal peak for revenue generation per employee. Since 1996, operating revenue per employee has improved significantly.

Air Canada performs aircraft maintenance, ground handling and other services for airlines and other customers. In 2000, these services generated over $200 million of revenue. The employees who perform this work are included in FTE employee counts.



* Air Canada and Canadian Airlines for full year 1999 and 2000.

On a combined basis, including Canadian Airlines revenues and employee counts for the periods prior to acquisition, operating revenue per employee in 2000 would have been 8 per cent higher than the 1999 combined level.

Operating Fleet

Air Canada's and Canadian Airlines' operating fleet, excluding Regional Airlines aircraft, at December 31, 2000, is as described below:

	Number of Aircraft [1]	Average Age of Aircraft (Years)	Owned	Capital Lease	Operating Lease [2]	On Order [3]	Options
Widebody Aircraft							
Airbus A340-500	–	–	–	–	–	5	10 [4]
Airbus A340-300	12	3.5	–	–	12	–	9 [4]
Airbus A330-300	4	1.0	–	–	4	4	9 [4]
Boeing 747-400	7	9.1	–	1	6	–	–
Boeing 767-300	28 [5]	8.8	–	3	25	4 [5]	–
Boeing 767-200	23	15.7	16	–	7	–	–
Narrowbody Aircraft							
Airbus A321	–	–	–	–	–	12	–
Airbus A320	47	9.1	21	1	25	3	–
Airbus A319	35	3.2	9	–	26	13	–
Boeing 737-200	43	20.3	1	10	32	–	–
DC-9	17	32.3	17	–	–	–	–
Canadair Regional Jet	25	5.2	2	–	23	–	–
Total Aircraft	241	11.6	66	15	160	41	28

(1) Excluding three Boeing 747-200, six DC-9 and one Boeing 737 aircraft which have been retired from service and were available for sale as at December 31, 2000.
(2) Air Canada retains a residual value interest in a significant number of leased aircraft through purchase options.
(3) On order aircraft includes 28 aircraft to be acquired under purchase contracts and 13 aircraft to be acquired under operating leases.
(4) Air Canada has the ability to convert the option aircraft into A340-300, A330-300, A340-500 or 600 aircraft, subject to certain conditions.
(5) Excluding one leased Boeing 767-300 aircraft which was delivered in December 2000 but which was not operational until early 2001.

During 2000, Air Canada and Canadian Airlines took delivery of two Airbus A330-300 and nine Boeing 767-300 aircraft, one of which was not operating until early 2001. The two Airbus A330 aircraft are on long-term lease and the nine Boeing 767-300 aircraft are on short-term leases ranging from two to five years. Certain of these Boeing 767 aircraft were added to replace eight DC-10 aircraft which were retired from Canadian Airlines' fleet in late 1999 to early 2000. As at December 31, 2000, the average age of the operating fleet was 11.6 years (7.7 years excluding DC-9 and Boeing 737 aircraft).

Air Canada has available for sale three Boeing 747-200, six DC-9 and one Boeing 737 aircraft which have all been retired from service.

At December 31, 2000, Air Canada's entire operating fleet, except for two DC-9 and eight Boeing 737 aircraft met the Stage 3 noise regulations, effective in the United States on December 31, 1999 and which are being implemented progressively in Canada. Three Boeing 737 aircraft are operated in northern Canada and are exempt from the Stage 3 noise regulations. The final date requiring all aircraft to be Stage 3 compliant in Canada is April 1, 2002, excluding northern Canada operations. The Corporation plans to install hushkits on two Boeing 737 aircraft in 2001. Any DC-9 and Boeing 737 aircraft that do not meet the Stage 3 noise regulations in Canada will not be operated beyond April 1, 2002.

The Regional Airlines operating fleet at December 31, 2000 is as described below:

	Total Number of Aircraft	Owned [1]	Operating Lease [2]	On Order
Regional Airlines Aircraft				
British Aerospace BAe 146	10	–	10	–
Fokker F28	30	28	2	–
de Havilland DHC-8-300	26	21	5	–
de Havilland DHC-8-100	63	51	12	–
Beech 1900D	5	5	–	–
Total Aircraft	134	105	29	–

(1) Including aircraft owned by the Corporation and its subsidiaries.
(2) Excluding five leased Jetstream aircraft, of which two were subleased to a third party and three were surplus.

Planned Aircraft Acquisitions

The table below outlines Air Canada's planned acquisition of aircraft in the 2001 to 2003 period as at December 31, 2000. These aircraft will either be acquired through committed purchases with corresponding financing or through committed operating leases.

Aircraft Type	2001 Purchase with Financing	2001 Lease	2002 Purchase with Financing	2002 Lease	2003 Purchase with Financing	2003 Lease	Total
Airbus A340-500	–	–	2	–	3		5
Airbus A330-300	4	–	–	–			4
Boeing 767-300	–	4			–		4
Airbus A320		–	–	3	–		3
Airbus A319	–	3	5	3	2		13
Airbus A321	5	–	7	–	–	–	12
Total	9	7	14	6	5	–	41

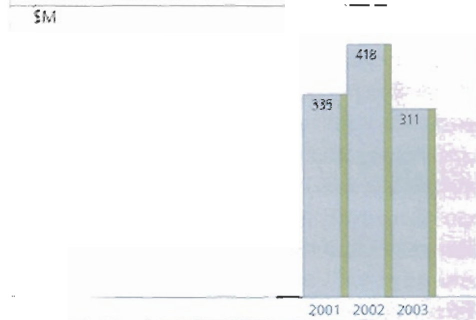
The Corporation has commitments for the delivery under long-term operating leases of four Boeing 767-300 and three Airbus A319 aircraft in 2001, as well as three Airbus A320 and three Airbus A319 aircraft in 2002. As these aircraft commitments are for delivery under operating leases, they are not included in the capital expenditures.

Planned Capital Expenditures and Financing

Air Canada has purchase agreements with Airbus for the acquisition of four twin-engine Airbus A330-300 aircraft in 2001. In addition, the Corporation will purchase a total of 12 Airbus A321 aircraft, five in 2001 and seven in 2002. Air Canada will be the first operator in Canada and the second in North America of the Airbus A321 aircraft. The Airbus A321 aircraft is the largest narrowbody aircraft in the Airbus family with 161 seats. As well, commitments are in place for the purchase of seven Airbus A319 aircraft, five in 2002 and two in 2003. Air Canada also has committed to acquire five new generation Airbus A340-500, two in 2002 and three in 2003. The Corporation will be a launch customer for the A340-500 series aircraft. The A340-500 aircraft, seating 264 passengers, will be the longest range airliner in the world capable of providing non-stop service on routes such as Toronto-Hong Kong on a year-round basis.

The Airbus aircraft Air Canada is acquiring will bring operational and maintenance cost savings compared to other fleet types through commonality with Airbus aircraft already operated by the airline.

PLANNED AND COMMITTED CAPITAL EXPENDITURES, AFTER COMMITTED FINANCING



The table below summarizes the Corporation's committed and planned capital expenditures, after committed aircraft financing, for the 2001 to 2003 period as at December 31, 2000.

($ millions)*	2001	2002	2003
Committed aircraft expenditures before committed financing	767	828	461
Committed aircraft financing	(745)	(901)	(518)
Net committed aircraft expenditures (proceeds) after financing	22	(73)	(57)
Planned expenditures for aircraft, engines, inventory, spare parts, modifications and refurbishments	113	291	118
Other planned or projected property and equipment expenditures	200	200	250
Planned and committed capital expenditures, after committed financing	335	418	311

* US dollar amounts are converted at the rate of CDN$1.50 per US dollar

Committed aircraft expenditures before committed financing represent progress as well as final payments for purchases of new aircraft assuming that Air Canada purchases all aircraft prior to any lease financing arrangement.

Committed aircraft financing represents 100 per cent financing commitments covering two Airbus A330-300 deliveries and a number of Airbus A319 and A321 aircraft up to US$384 million. All other aircraft purchases have committed financing of 85 per cent. The financing amounts shown assume that the financing facilities are fully utilized under sale and leaseback arrangements. Subject to financial conditions, Air Canada may purchase rather than lease some of these aircraft.

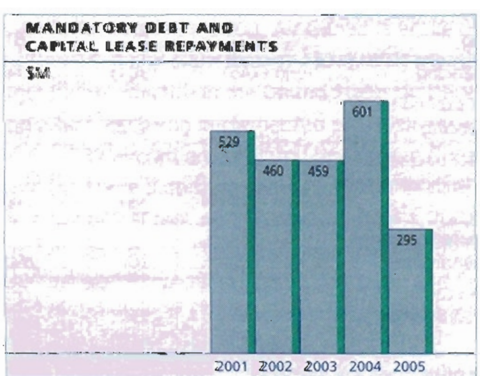
At December 31, 2000, net committed aircraft expenditures after financing amounted to $22 million in 2001 with committed proceeds of $73 million and $57 million in 2002 and 2003 respectively. The net proceeds in 2002 and 2003 represent the return of a portion of aircraft progress payments made by Air Canada in prior years, following the planned lease financing of the aircraft.

Other planned or projected property and equipment expenditures are for committed, planned or projected capital spending on information technology projects, airport improvements, maintenance facility upgrades, ground and computer equipment, facilities and expenditures by subsidiaries. The Corporation has introduced measures to reduce its uncommitted capital spending in 2001. Other property and equipment expenditures do not include any amounts relating to a long-term information technology services agreement pending finalization of the bid process and selection of the supplier.

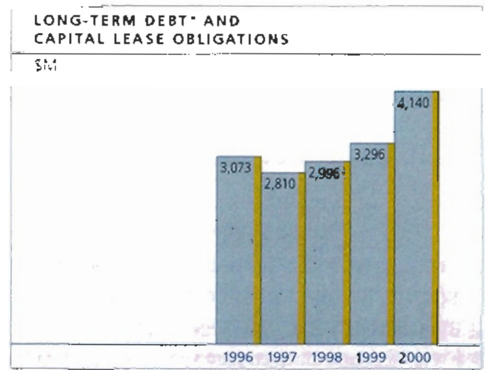
All uncommitted capital expenditures are subject to change based on management's assessment of future market and financial conditions.

In 2001, the Corporation plans to remove the equivalent of up to eight widebody aircraft from the operating fleet through sublease or sale and potentially parking older, less efficient narrowbody aircraft. The Corporation plans to remove from service four Boeing 737, two DC-9 and 10 Fokker F28 aircraft in 2001.

The accompanying chart summarizes Air Canada's mandatory debt and capital lease principal repayments for the years 2001 to 2005, at December 31, 2000.



Assuming the 41 committed future aircraft deliveries are all acquired under operating leases, aircraft rent expenses are expected to amount to approximately $950 million in 2001, $1,025 million in 2002 and $1,100 million in 2003, net of planned aircraft retirements. Planned depreciation, amortization and obsolescence expense, reflecting projected capital expenditures at December 31, 2000 is expected to amount to $490 million in 2001, $550 million in 2002 and $590 million in 2003. The aircraft rent and depreciation expense estimates are subject to change depending upon decisions regarding aircraft fleet, planned or projected capital expenditures and asset dispositions.



* Including subordinated perpetual debt and current portion of long-term debt

At year-end, 30 per cent of the Corporation's aircraft by number (including retired aircraft but excluding Regional Airlines aircraft) or 17 per cent by fair market value were owned and unencumbered. These aircraft represent a potential future source of financing through sale or sale and leaseback arrangements.

Risk Management

The Corporation manages its exposure to changes in interest rates, foreign exchange rates and jet fuel prices through the use of various derivative financial instruments for the purpose of hedging existing commitments or obligations, not for generating trading profits. Most hedging takes place within a one-year time horizon and is principally in support of cash management activities. Longer term hedging is done infrequently and essentially supports financing activities.

The Corporation has entered into interest rate swap agreements in order to manage the interest rate exposure associated with certain long-term debt obligations. At December 31, 2000, US$537 million of debt was in floating rate US dollars and approximately 16 per cent of the planned 2001 interest rate exposure on this floating rate debt was effectively hedged with short-term interest rate contracts. Of the Corporation's Canadian dollar debt, $537 million was at floating interest rates with no interest rate contracts in place. The Corporation's cash position, which is invested in highly rated interest bearing instruments, provides a partial effective hedge against interest rate movements on the floating rate debt to the extent short-term US and Canadian interest rates move in tandem. Short-term interest rates on cash balances may be periodically effectively hedged depending upon market conditions. At December 31, 2000, the Corporation held short-term interest rate agreements fixing only a nominal amount of its cash and cash equivalent investment portfolio for 2001. Movements in short-term interest rates can affect financial results due to Air Canada's floating rate debt position and short-term investment portfolio. Taking into account interest rate hedging at December 31, 2000, and projected short-term investments and planned debt repayments, a one percentage point change in short-term interest rates would have an estimated $7 million impact on net interest expense in 2001.

Based on book value, the weighted average cost of the Corporation's long-term debt and capital lease obligations (including Canadian Airlines debt for the period July to December 2000) was 8.1 per cent in 2000, up from 7.7 per cent in 1999. The higher weighted average cost of debt reflects, primarily, increased interest expense caused by higher US interest rates and a stronger Japanese yen, partially offset by weaker Swiss and German currencies. The higher weighted average cost also reflects relatively higher costs for Canadian Airlines debt in the July to December 2000 period.

The Corporation also manages foreign exchange exposure through the use of options, forward contracts and cross-currency swaps. During 2000, the Corporation purchased foreign exchange contracts that effectively converted 174 million Swiss franc debt into US dollars and the remaining 12 million Swiss franc debt into Canadian dollars. At December 31, 2000, approximately 5 per cent of the balance sheet exposure on Japanese yen debt was covered by short-term foreign exchange option contracts. No foreign exchange currency contracts were in place covering the principal amount of US debt. Aircraft assets, recorded on the balance sheet at historical exchange rates at the time of acquisition, are essentially US dollar-based assets which can provide a longer term economic hedge against US dollar currency movements. Cross-currency swap arrangements were also in place converting $405 million of fixed rate Canadian debt into floating rate Japanese yen debt in order to benefit from surplus Japanese yen cash flows and lower yen interest rates. Deutsche mark debt of 450 million was also swapped to Canadian dollar floating rate debt to minimize foreign exchange fluctuations and lock in required repayment amounts. At December 31, 2000, taking into account the coverage described above, only the principal amounts relating to US$989 million of US dollar debt and swap transactions and 43 billion of Japanese debt and long-term swap transactions were exposed to foreign exchange fluctuations. The principal amount of subordinated perpetual debt is not considered to be subject to economic foreign exchange risk, since the requirement to repay the principal is only upon liquidation, if ever, of the Corporation.

Ongoing foreign exchange exposure on interest obligations denominated in European currencies are fully covered by surplus cash flows. Annual Japanese yen cash flow surpluses provide a natural hedge which more than cover yen interest and principal payments. Air Canada periodically sells forward surplus foreign currency cash flows depending upon market conditions. At December 31, 2000, the Corporation had entered into foreign exchange contracts to effectively hedge a portion of its planned 2001 Japanese yen surplus cash flows.

Air Canada has an ongoing operational requirement for US dollars to cover various expenses such as fuel, aircraft materials, interest and aircraft lease payments as well as debt repayments. The Corporation generally obtains US dollars from operations as well as by buying dollars on the spot and forward exchange markets and through the conversion of other foreign currency surpluses into US dollars. At December 31, 2000, a nominal amount of the net projected operational requirements for US dollars in 2001 was covered by forward exchange contracts. With greater operations to the United States in 2000, Air Canada generated increased US dollar cash flows to better cover these requirements.

A one cent improvement in the value of the Canadian dollar compared to one US dollar (for example, an improvement from $1.50 to $1.49 for one US dollar) is estimated to increase planned operating income by approximately $8 million and reduce non-operating expense by $3 million in 2001. Conversely, a one cent deterioration would generally have the opposite effect.

Aircraft fuel is a major expense to the Corporation. The Corporation enters into contracts with credit worthy financial intermediaries, not exceeding two years, to manage its exposure to jet fuel price volatility. As at December 31, 2000, the Corporation had effectively hedged approximately 26 per cent of its anticipated 2001 fuel consumption. In January 2001, the Corporation reduced its hedging position and as at February 6, 2001, had effectively hedged approximately 15 per cent of its anticipated 2001 fuel consumption through various financial agreements for heating oil or WTI crude oil. This coverage translates into an equivalent WTI price of $30.89 per barrel for 2001. Based on 2000 fuel volumes and taking into account the historic movement of jet fuel spreads relative to WTI crude oil, a US$1 per barrel movement in the price of crude oil would result in an approximate CDN$45 million change in 2001 fuel expense as compared to combined fuel expense for Air Canada and Canadian Airlines in 2000, net of fuel hedges.

Sensitivity of Airline Results

Financial results of the Corporation are subject to many different internal and external factors which can have a significant impact on operating income and net income. In order to provide a general guideline, the table below describes, on an indicative basis, the financial impact that changes in operating assumptions would generally have on the 2001 Corporation's consolidated results. The guidelines have been derived from 2000 combined levels of activity and makes use of management estimates. The impacts are not additive, do not reflect the interdependent relationship of the elements and may vary significantly from actual results due to factors beyond the control of the Corporation.

Key Variable	Routes	2000 Measure	Sensitivity Factor	Estimated 2001 Operating Income Impact	Estimated 2001 Net Income Impact
Revenue Measures				($ millions)	($ millions)
Passenger yield per RPM (cents)	System	20.4	1% change in yield per RPM	83	49
	Canada	26.2		37	22
Traffic (RPMs) (millions)	System	44,968	1% change in traffic	73	43
	Canada	15,738		33	20
Passenger load factor (%)	System	70.9	1 percentage point change	103	61
RASM (cents)	System	14.5	1% change in RASM	78	46
Cost Measures					
Labour & benefit expenses ($ millions)		$2,978	1% change	30	18
Fuel – WTI price (US$/barrel)		US$30.21	US$1/barrel change to WTI (1)	45	27
Fuel – Jet fuel price (CDN cents/litre)		38.3	1% change	17	9
Cost per ASM (2) (cents)		16.8	1% change	107	63
Currency & Interest Rates					
Canada to US exchange (CDN$)		$1.50	1¢ change (e.g. $1.50 to $1.49 CDN dollar for one US dollar)	8 (3)	6
Floating US & Canadian interest Rates		CDN 6.50% US 7.25%	1 percentage point change in floating interest rates	0 (3)	4

(1) Assumes jet fuel spreads change in relation to WTI based on historical trends
(2) Excludes non-recurring items.
(3) Pre-tax impact is $11 million for a 1¢ change in the Canada to US exchange rate and $7 million for a 1 percentage point change in floating interest rates.

Outlook

The Corporation expects to achieve $700 million of annual synergies through revenue gains and cost reductions resulting from the Canadian Airlines acquisition and integration, as compared to the separate operations of the airlines in 1999. Management estimates that approximately 45 per cent of these synergies were realized in 2000 and that substantially all of these synergies will be realized by the end of 2001. Management expects to achieve these synergies mainly in the areas of capacity redeployment, customer service, operations and employee reductions.

Based on trends which emerged in the fourth quarter of 2000, the Corporation faces a slowing economy, increasingly intense domestic competition and volatile crude oil prices. As a result, Air Canada is introducing a number of scheduling, fleet and labour-related measures in 2001 to realign capacity with projected demand and to improve financial performance.

In early February 2001, the Corporation announced its intention to maintain its 2001 available seat mile capacity at 2000 levels and to focus on maximizing load factors, yields and profitability. As part of this initiative, the Company is decreasing the size of aircraft operated or the frequency of aircraft operations on certain underperforming routes. In 2000, load factors improved on domestic routes, where large capacity surpluses were removed. In 2001, Air Canada will suspend certain underperforming international routes, as well as reduce low season frequency on other international routes. Air Canada will also realign its fleet in response to these capacity adjustments. Specifically, the Corporation plans to (i) offset the addition of eight new widebody aircraft scheduled for delivery with the disposition of up to eight older widebody aircraft through sale or sublease and potentially parking older, less efficient narrowbody aircraft, (ii) accelerate the retirement of 30 Fokker F28 aircraft operated by the Regional Airlines and (iii) postpone the Company's planned replacement of certain of its narrowbody fleet, except for replacements by committed aircraft orders.

In the course of 2001 and early 2002, the Corporation also plans to lower employee counts by approximately 3,500 employees mainly through voluntary separation programs. The Corporation expects employee reductions to be substantially completed by the fall of 2001.

Air Canada is proactively adjusting its operations based on the assumption that the economic slowdown already in place in the United States will have a significant effect on the Canadian economy and travel demand. To the extent that this scenario does not fully materialize, Air Canada will retain the flexibility to adjust capacity and operations. In the event however, of a more unfavourable economic climate, the Corporation will continue to review its operations and will consider further measures to reduce capacity and infrastructure, in line with passenger and cargo demand.

In the summer of 2000, the Corporation integrated the schedules of Air Canada and Canadian Airlines and realigned operations at airports without the benefit of intermingling agreements for its key customer sales and service personnel and without a common computer reservations system. As a result of service deficiencies which occurred in 2000, the Corporation added over 2,000 personnel to compensate for the lack of labour and systems integration. With the introduction of an intermingling agreement for customer sales and service employees and the successful cutover to a common passenger reservations system, significant labour and integration synergies were achieved, resulting in surplus employees and the ability to offer voluntary severance packages to employees made surplus by integration.

During 1999 and 2000, the Corporation successfully concluded long-term labour agreements with all of its major unions, with the exception of Air Canada flight attendants represented by the Canadian Union of Public Employees (CUPE). These agreements included: a four-year collective agreement with the Air Canada Pilots' Association (ACPA); agreement extensions for up to three years with the Canadian Auto Workers (CAW) representing sales and service agents, with the Canadian Union of Public Employees (CUPE) covering Canadian Airlines' flight attendants and with the International Association of Machinists and Aerospace Workers (IAMAW) covering both Air Canada and Canadian Airlines maintenance, cargo and airport ramp service personnel which included wage increases to 2005. A work force integration agreement was concluded with the CAW and commenced in October 2000. Intermingling of work between Air Canada and Canadian Airlines IAMAW employees began in February 2001. Negotiated settlements covering common work rules for the CAW and CUPE (Canadian Airlines) labour groups have also been concluded. In 2001, Air Canada has one major labour agreement to be renewed in October 2001 covering over 5,300 Air Canada flight attendants represented by CUPE.

In September 2000, Air Canada and Canadian Airlines were declared to be a common employer by the Canada Industrial Relations Board (CIRB). A representation vote is being conducted between the Air Canada pilots represented by ACPA and the Canadian Airlines pilots represented by the Air Line Pilots Association (ALPA) under the direction of CIRB. This vote will determine which union will represent the combined work force.

The largest benefit from intermingling is being achieved through the CAW agreement of October 2000 followed by the IAMAW intermingling in February 2001. Intermingling of Air Canada and Canadian Airlines pilot groups and flight attendant groups, along with common unions and seniority lists, would streamline operations and contribute positively to further integration savings benefits.

On January 01, 2001, Air Canada and Canadian Airlines International Ltd. were amalgamated and continued as one corporation, with the amalgamated entity being known as Air Canada. The amalgamation principally relates to the legal status of the Corporation. Air Canada has applied to Transport Canada for a single Air Operator Certificate (AOC) which will allow for managerial control of all operations to reside with one organization. In order to meet the requirements of a single AOC, standard pilot operating procedures and training must be completed, along with standardized procedures and training for all flight attendants, maintenance, flight dispatch and other personnel. It is expected that Air Canada will be granted a single AOC during 2001 and all required training, manuals and procedures will be completed by mid-2001.

Effective January 01, 2001, Air Canada's Regional Airlines were combined as one legal entity, Air Canada Regional Inc. The amalgamated entity will continue to carry on business under the brand names of AirBC, Air Ontario, Air Alliance, Air Nova and Canadian Regional. On January 31, 2001, Air Canada Regional was granted a single AOC. The airline will operate as separate divisions until all operational staff are trained and utilize a common set of procedures, which is targeted for April 2001. The Canada Industrial Relations Board granted common employer status to Air Canada Regional in October 2000. Air Canada Regional will begin bargaining discussions with its union groups in the first quarter of 2001. The majority of negotiations are expected to be concluded in 2001. The consolidation of the Regional Airlines is expected to provide longer term synergy benefits in the form of increased scheduling efficiencies, reduced overhead and administrative costs and operational synergies.

Aeroplan, Air Canada's frequent flyer plan, has over 6 million members, including former Canadian Airlines' Canadian Plus members. In August 2000, Air Canada announced its intent to reorganize Aeroplan as a new division with the mandate to more fully develop Aeroplan as an international leader in customer loyalty management. This was the first of several new business initiatives Air Canada is undertaking to create new profit centers within the Corporation. The Corporation is considering the merits of establishing a separate corporate entity and launching an initial public offering for Aeroplan, however no decision has been made in this regard.

In November 2000, Air Canada announced its intention to form Air Canada Technical Services as a division of Air Canada, to compete on a global basis as an aircraft maintenance, repair and overhaul profit center. Air Canada Technical Services is responsible for the maintenance, engineering and repair of Air Canada's aircraft fleet and provides maintenance services to numerous third party airlines. The mandate for the new division is to enhance shareholder value by competing for profitable third party contracts either directly or through joint ventures. The Corporation is currently establishing criteria for the operation of the profit center and may consider joint venture arrangements or alternate business structures for the evolution of this business.

Air Canada has an over 70 per cent share of the Canadian domestic passenger travel market based on scheduled capacity for the first quarter of 2001 and had, in 2000, an over 50 per cent share of the Canada-US transborder market as measured by passenger sales by travel agents in Canada. In the domestic market, Air Canada competes mainly with five scheduled and charter airlines and outside Canada with more than 40 international scheduled and charter carriers. During the past several years, a number of low-cost, low-fare competitors have commenced service in Canada on domestic routes or expanded existing services through new scheduled or charter operations. Since the announcement of the Canadian Airlines acquisition, low-cost carriers in Canada have accelerated expansion plans on the domestic market. In 2000, WestJet Airlines (WestJet), a low-cost low-fare carrier based in western Canada, introduced new services from Hamilton to Thunder Bay, Winnipeg, Ottawa and Moncton. WestJet has also announced plans to commence new non-stop services in 2001 between Ottawa and Calgary. WestJet has a fleet of 23 Boeing 737-200 aircraft and has announced plans to add four Boeing 737-700 aircraft in 2001, with a further six Boeing 737-700s in 2005. WestJet also has 26 Boeing 737-600 or 700 aircraft on order for 2003 to 2005. In late January 2001, two airlines in Canada, Canada 3000 Inc. (Canada 3000) and Royal Aviation Inc. (Royal) announced an agreement whereby Canada 3000 would acquire the shares of Royal, subject to certain conditions. The carriers announced that the combined airline would have a fleet of 34 aircraft, with 10 more aircraft on order and would have had combined annual revenues of over **$1** billion in the preceding year. In September 2000, a new low-cost air carrier, CanJet Airlines (CanJet), commenced operations based in Halifax, Nova Scotia to several destinations in eastern and central Canada. CanJet currently operates six Boeing 737-200 aircraft. Another airline competitor, Roots Air, has announced plans to commence services beginning in late March of 2001, offering premium services initially on the Toronto-Calgary/Vancouver routes with planned expansion to Montréal and Los Angeles by June 2001.

Pursuant to an undertaking with the Competition Bureau, Air Canada is prohibited from introducing a domestic discount airline on routes which originate or terminate in eastern Canada until September 30, 2001. Air Canada is however permitted to commence a discount airline operating in western Canada or on transborder routes at any time. While Air Canada had previously announced plans to start up a new low-fare airline in 2000, it will not do so until labour work rules, conditions and aircraft fleet size can be negotiated which would make the low-fare operation economically viable.

In July 2000, the Government of Canada passed legislation to govern the competitive airline environment in Canada and ensure protection for consumers. The legislation increased the powers of the Canadian Transportation Agency with respect to domestic air fares and cargo rates on non-competitive routes as well as domestic terms and conditions of carriage. Other measures included broader notice provisions on discontinuance of service, extension of the Official Languages Act to Air Canada's airline subsidiaries and the appointment of an independent commissioner to review certain complaints made against airlines. Additionally, the legislation granted new powers to the Competition Bureau in respect of anti-competitive airline behaviour and gave travel agents the ability to negotiate collectively domestic base commissions with an airline that, together with its affiliates, accounts for at least 60 per cent of the domestic revenue passenger kilometers. The legislation also incorporated undertakings made to the Competition Bureau whereby Air Canada agreed, in connection with the acquisition of Canadian Airlines, to take certain steps and to accept certain conditions in order to promote and maintain airline competition in Canada. They included the surrender of a limited number of slots and airport facilities, limitations on the operation of a proposed discount airline as indicated above and engagements respecting frequent flyer programs, travel agent commission overrides and the offering for sale of Canadian Regional Airlines, amongst others. Also included in the legislation are commitments made by Air Canada in December 1999 to the Minister of Transport regarding the provision of domestic service to small communities served by Air Canada, Canadian Airlines or any of their wholly-owned subsidiaries for a three year period as well as commitments to employees to ensure that there are no involuntary layoffs or involuntary relocations prior to March 2002. The legislation also raised the limit on individual share ownership in Air Canada from 10 to 15 per cent.

In October 2000, in response to a complaint from CanJet, the Commissioner of the Competition Bureau issued a temporary order requiring that Air Canada cease and desist from offering certain competitive discount fares on five routes on which CanJet also operated. The order was subsequently extended on October 31, 2000 and November 24, 2000 on three of these routes. As a result, Air Canada was prohibited from offering these fares until December 31, 2000. In late February 2001, following discussions with the Competition Bureau, Air Canada withdrew certain discount fares on three routes operated by CanJet. Also, in February 2001, the Competition Bureau released for consultation draft Enforcement Guidelines outlining the approach it proposes to take in enforcing the abuse of dominance provision of the Competition Act for the airline industry and has requested comments from interested stakeholders by May 2001.

In early March 2001, the Competition Bureau announced that it had asked the Competition Tribunal for an order prohibiting Air Canada from engaging in anti-competitive practices directed against CanJet and WestJet. In an application under the abuse of dominance provisions of the Competition Act, the Competition Bureau is seeking an order prohibiting Air Canada from charging fares on flights on certain routes in eastern Canada that do not cover its "avoidable costs" of providing the service. Air Canada subsequently announced that it intends to vigorously challenge the Competition Bureau's application for an order which, if granted, would prohibit Air Canada from matching fares or otherwise being price competitive on certain routes operated by CanJet or WestJet. Air Canada also disagrees with the Competition Bureau's finding that Air Canada engaged in anti-competitive practices directed against the two carriers and its interpretation of "avoidable costs". In order to resolve these issues on a timely basis, Air Canada has agreed with the Competition Bureau to have an expedited hearing before the Competition Tribunal for clarification of certain rules relating to pricing behaviour in the domestic market including, in particular, the application of the "avoidable cost" test set out in the Regulations respecting anti-competitive acts. It is not possible to determine the potential outcome of the initiatives by the Competition Bureau.

In March 2001, the Canadian Transportation Agency rendered its first pricing decision concerning the reasonableness of discount fares offered in respect of a non-competitive domestic service following a complaint filed against Air Canada in August 2000. The Canadian Transportation Agency determined that the lowest return fare offered by Air Canada on its service between Prince Rupert and Vancouver at the time of the complaint was unreasonable when compared to the lowest return fares on a comparable competitive route. It intends to direct Air Canada to amend its tariff by reducing the discount fare for the same period and in the same proportion regarding seat availability as the lowest return fares on the comparable competitive route. Air Canada strongly disagrees with these findings and intends to file representations to the Canadian Transportation Agency and take any necessary court action. Approximately 20 pricing complaints have been forwarded to Air Canada for response since legislation was passed in July 2000 enlarging the jurisdiction of the Canadian Transportation Agency over domestic pricing matters.

In February 2001, the Minister of Transport announced the launch of an international air services policy review. This review initially involves consultation sessions with industry stakeholders. The objective of the review is to liberalize Canada's policy for scheduled international air services including how Canada approaches the negotiation and management of air traffic rights with other countries. This new policy is expected to come into effect at the end of October 2001, following completion of the consultation phase.

Air Canada will continue to focus on international expansion opportunities with its Star Alliance partners through codeshare and other commercial arrangements. Air Canada's participation as a founding member of Star Alliance offers significant long-term potential to improve revenues and reduce costs. The 15 Star Alliance airlines had combined revenues of over US$63 billion in 1999 and carried over 295 million passengers. Star Alliance carriers offer service to over 800 cities around the globe in more than 130 countries. In 2000, Singapore Airlines, Austrian Airlines, British Midland and Mexicana Airlines joined Star Alliance. The alliance provides customers with a high level of service between network connection points together with mutual recognition of the status of the best customers, reciprocal participation in frequent flyer programs, use of airport lounges and other product enhancements. Additionally, the carriers benefit from cost synergies through common utilization of airport terminal facilities, sales offices and joint purchasing arrangements. In 2000, Air Canada's interline passenger revenues from Star Alliance partners grew by 20 per cent to over $450 million and continued growth is expected in 2001.

In the United States, there have been a number of airline acquisition proposals which, subject to regulatory approval, would result in a significant consolidation of the US airline industry. United Airlines, Air Canada's Star Alliance partner and the largest US carrier as measured by ASM capacity, has offered to acquire the operations of the sixth largest US carrier, US Airways. AMR Corporation, the parent of American Airlines, has offered to acquire most of the assets of Trans World Airlines (TWA) which filed for bankruptcy protection in January 2001. Additionally, it has been reported that the third largest carrier, Delta Air Lines, is in discussion with the fifth largest US carrier, Continental Airlines, and the fourth largest US carrier, Northwest Airlines, regarding a potential business combination. These acquisition proposals require regulatory approval by the US Department of Transportation and the US Department of Justice. If the United Airlines-US Airways transaction is culminated, Air Canada envisages that there could be potential benefits through expansion of its Star Alliance network in the United States. However, these potential benefits could be adversely impacted by consolidation activities of other airlines.

In late January 2001, Air Canada and the Greater Toronto Airports Authority (GTAA) signed a comprehensive memorandum of understanding regarding Air Canada's future operations and the development of Lester B. Pearson International Airport (Pearson), Air Canada's main hub. The GTAA commenced construction of a major development project at Pearson to replace Air Canada's Terminals 1 and 2 with a new passenger terminal as well as a new cargo infield area and an additional runway. Air Canada has finalized plans with the GTAA for Air Canada and its Star Alliance partners to occupy the first phase of the new passenger terminal, "Terminal New", at Pearson by late 2003 / early 2004 with the balance of the operation relocating to Terminal New in 2005. The agreement resolves all outstanding issues with the GTAA, in regard to Air Canada's concerns relating to operational, financial and development issues. Pursuant to this memorandum of understanding, Air Canada sold certain of its existing facilities and rights at Pearson to the GTAA for $130 million and may receive an additional $20 million for future construction at Pearson. The GTAA has also announced the imposition of an Airport Improvement Fee to fund a portion of its capital expenditures commencing June 1, 2001.

Air Canada has invested significantly in information technology as a means to improve customer service, lower costs and improve productivity. These investments will continue in the coming years especially in the areas of internet, e-commerce and web based distribution systems. Air Canada is currently evaluating contract proposals for a long-term information technology services agreement following the expiry of its current agreement in July 2001, subject to Air Canada's right to extend, pursuant to the terms of the current agreement. The selection of Air Canada's information technology supplier is expected to be made in the second quarter of 2001.

In December 2000, the Canadian Institute of Chartered Accountants (CICA) issued a draft proposal for the reporting of financial instruments and similar items. Under this proposal virtually all financial instruments (defined as cash, equity instruments, or specific types of contractual financial obligations) would be reported at current market values with any gains or losses resulting from the changes in value being included in the current period's income. One of the draft recommendations would require the Corporation to record, in current income, changes in the market value of long-term and perpetual debt obligations denominated in foreign currencies. The CICA is requesting comments on the draft proposal by mid-year 2001. Potential implementation of a new accounting standard could follow in late 2001 or in 2002.

The airline industry is subject to a number of influences over which it has limited or no control including fuel prices, weather, competition and economic conditions as well as regulatory factors and government policies and decisions. Economic conditions in Canada are expected to slow in 2001 driven largely by weaker economic conditions in the United States.

Over the past year, Air Canada has focused on integrating the schedule and operations of Canadian Airlines and on establishing a solid long-term labour environment for integrated operations. With many of the integration activities completed, the focus in 2001 is to limit capacity growth, optimize revenue generation and to achieve expense reductions through greater fleet utilization, realization of synergy benefits of integration and increased use of technology. The major rise in crude oil and jet fuel prices in 1999 and 2000 will continue to be a significant factor with continuing high fuel costs forecast in 2001. The Corporation introduced a 6 per cent domestic passenger fare increase in January 2001 to partially mitigate the effect of the high cost of fuel.

The year 2001 challenge is to realize the full synergy potential of Air Canada and Canadian Airlines. Air Canada remains committed to pursuing initiatives to enhance shareholder value and expects to realize, with intermingling of labour forces, a common computer reservations system and, in 2001, a single AOC, the planned synergy benefits from the Canadian Airlines acquisition. High fuel prices, coupled with an uncertain economic environment and increased competition by low-fare airlines will continue to have an adverse impact in 2001. However, the Corporation remains focused on making the strategic decisions and implementing required actions to increase financial returns and shareholder value over the longer term.

This discussion contains certain forward-looking statements, which involve a number of risks and uncertainties. Although the Company has completed the majority of its key integration milestones in connection with the Canadian Airlines acquisition, some elements have yet to be implemented and many of the benefits may only be realized over time, if at all. Management expects that substantially all of the benefits will be realized by the end of 2001 and that the revenue enhancements and cost savings arising from the integration will ultimately be up to $700 million annually. These estimates are based upon numerous assumptions, some of which may prove to be incorrect, and there can be no assurance that all the benefits will be realized or realized in this time period. For example, the savings from voluntary separation programs, which offer employees incentives to terminate their employment, may be realized later than expected. In addition, the estimated synergies are based on the revenues and costs of the separate operations of Air Canada and Canadian Airlines as they existed, in 1999, prior to the acquisition. Future economic, competitive, employee relations and regulatory environments will be different from those prior to the acquisition, making it difficult to measure whether the amount of expected revenue enhancements or cost savings has been achieved. For instance, if competition in the airline industry increases, Air Canada may have to incur additional marketing and distribution costs, making it difficult to determine whether the Company's targeted reduction in these expenses under the integration program has been achieved. Even if the Corporation does achieve its synergy objectives, such synergies may not translate directly to the Corporation's future operating profitability, which is dependent upon numerous factors, many of which are beyond the Corporation's control. For instance, if reduced levels of economic activity adversely affect airline business volume, this may offset the revenue enhancements achieved in the integration, or have the effect of increasing expenses relative to operating revenues. As a result of many factors including labour negotiations, fuel prices, industry restructuring, the economic environment in general including foreign exchange and interest rates, the airline competitive and pricing environment, industry capacity decisions, new entrants, government regulations and government mandated restrictions on operations and pricing as well as external events, actual results could differ from expected results and the differences could be material.

Management's Report

The consolidated financial statements contained in this annual report have been prepared by management in accordance with generally accepted accounting principles and the integrity and objectivity of the data in these financial statements are management's responsibility. Management is also responsible for all other information in the annual report and for ensuring that this information is consistent, where appropriate, with the information and data contained in the financial statements.

In support of its responsibility, management maintains a system of internal control to provide reasonable assurance as to the reliability of financial information and the safeguarding of assets. The Corporation has an internal audit department whose functions include reviewing internal controls and their application, on an ongoing basis.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control and exercises this responsibility through the Audit Committee of the Board, which is composed of directors who are not employees of the Corporation. The Audit Committee meets with management, the internal auditors and the external auditors at least four times each year.

The external auditors, PricewaterhouseCoopers LLP, conduct an independent audit, in accordance with generally accepted auditing standards, and express their opinion on the financial statements. Their audit includes a review and evaluation of the Corporation's system of internal control and appropriate tests and procedures to provide reasonable assurance that, in all material respects, the financial statements are presented fairly. The external auditors have full and free access to the Audit Committee of the Board and meet with it on a regular basis.

R Pet

M. Robert Peterson
Executive Vice President
and Chief Financial Officer

RAMilton

Robert A. Milton
President and
Chief Executive Officer

Auditors' Report

To the Shareholders of Air Canada:
We have audited the consolidated statement of financial position of Air Canada as at December 31, 2000 and 1999 and the consolidated statements of operations and retained earnings (deficit) and cash flow for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2000 and 1999 and the results of its operations and the changes in its cash flow for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants
Montréal, Québec

January 31, 2001

Consolidated Statement of Operations and Retained Earnings (Deficit)

(in millions except per share figures)

Year ended December 31	2000	1999
Operating revenues		
Passenger	$ 7,949	$ 5,520
Cargo	542	387
Other	792	536
	9,283	6,443
Operating expenses		
Salaries and wages	2,160	1,503
Benefits	410	257
Aircraft fuel	1,371	622
Depreciation, amortization and obsolescence	405	311
Commissions	521	420
Food, beverages and supplies	367	264
Aircraft maintenance, materials and supplies	464	334
Airport and navigation fees	657	492
Aircraft rent	705	513
Other (note 1j)	1,959	1,350
	9,019	6,066
Operating income before the undernoted item	264	377
Non-recurring labour expenses (note 1q)	178	-
Operating income	86	377
Non-operating income (expense) (note 6)		
Net interest expense	(210)	(154)
Amortization of deferred foreign exchange	(24)	(18)
Gain on sale of investments and other assets	15	57
Other	6	(1)
	(213)	(116)
Income (loss) before income taxes	(127)	261
Recovery of (provision for) income tax (note 12)	45	(121)
Income (loss) for the year	(82)	140
Retained earnings (deficit), beginning of year as originally reported	(265)	152
Adjustments relating to changes in generally accepted accounting principles (note 18)	(329)	(289)
Deficit, beginning of year as restated	(594)	(137)
Charge relating to share buy back (note 11)	-	(630)
Deficit, end of year	$ (676)	$ (627)
Earnings (loss) per share		
Basic	$ (0.69)	$ 0.76
Fully Diluted	$ (0.69)	$ 0.75

See accompanying notes.

Consolidated Statement of Financial Position

(in millions)

December 31		2000		1999
Assets				
Current				
Cash and cash equivalents (note 1d)	$	437	$	521
Accounts receivable		909		443
Spare parts, materials and supplies		403		228
Prepaid expenses		33		18
Future income taxes (note 12)		436		48
		2,218		1,258
Property and equipment (note 3)		4,174		3,220
Future income taxes (note 12)		239		125
Deferred charges (note 4)		1,319		1,286
Goodwill, net of amortization (note 1a)		527		35
Other assets (note 5)		1,244		872
	$	9,721	$	6,796
Liabilities				
Current				
Bank indebtedness and short-term loans	$	264	$	–
Accounts payable and accrued liabilities		2,269		1,045
Advance ticket sales		498		341
Current portion of long-term debt and capital lease obligations		529		114
		3,560		1,500
Long-term and subordinated perpetual debt and capital lease obligations (note 7)		3,611		3,182
Future income taxes (note 12)		75		86
Other long-term liabilities		1,175		807
Deferred credits (note 10)		984		858
		9,405		6,433
Shareholders' Equity				
Share capital (note 11)		977		975
Contributed surplus (note 11)		15		15
Deficit		(676)		(627)
		316		363
	$	9,721	$	6,796

See accompanying notes.

Approved by the Board:

Robert A. Milton
President and Chief Executive Officer

John F. Fraser, OC
Chairman of the Board

Consolidated Statement of Cash Flow

(in millions except per share figures)

Year ended December 31	2000	1999
Cash flows from (used for)		
Operating		
Income (loss) for the period	$ (82)	$ 140
Adjustments to reconcile to net cash provided by operations		
Depreciation, amortization and obsolescence	405	311
Gain on sale of investments and other assets (note 6)	(15)	(57)
Future income taxes	(42)	103
Pension funding less than (greater than) pension expense	55	(57)
Deferred group health/life retirees expense	28	22
Amortization of deferred foreign exchange	24	18
Amortization of deferred gains	(31)	(16)
Increase in accounts receivable	(192)	(38)
Decrease (increase) in spare parts, materials and supplies	(84)	18
Increase in accounts payable and accrued liabilities	292	100
Decrease in advance ticket sales	(103)	(15)
Aircraft lease payments in excess of rent expense	(62)	(96)
Contributions on commercial agreement extensions (note 1m & 10)	–	298
Deferred financing charges	–	(68)
Other	(78)	17
	115	680
Financing		
Issue of share capital (note 11)	2	137
Share buy-back (note 11)	–	(1,100)
Issue of convertible subordinated debentures (note 8)	–	141
Long-term borrowings	761	431
Reduction of long-term debt	(490)	(117)
Other	(16)	(7)
	257	(515)
Investing		
Proceeds from sale and leaseback of assets	292	137
Proceeds from sale of investments and other assets	45	80
Additions to property and equipment, net of recovered progress payments	(587)	(271)
Acquisition of CAIL net of cash acquired (note 2)	(125)	(6)
Investments and advances	(81)	50
	(456)	(10)
Increase (decrease) in cash and cash equivalents	(84)	155
Cash and cash equivalents, beginning of year	521	366
Cash and cash equivalents, end of year	$ 437	$ 521
Cash flow per share from operations		
Basic	$ 0.96	$ 3.71
Fully diluted	$ 0.87	$ 3.61

See accompanying notes.

1. Significant Accounting Policies

Nature of Operations

Air Canada is Canada's largest domestic and international airline, providing scheduled and charter air transportation for passengers and cargo. Air Canada offers air transportation on routes authorized by the Government of Canada and the foreign governments concerned. The Corporation's route network, including Canadian Airlines International Ltd. and the regional airline subsidiaries, serve 150 destinations including 68 cities in Canada, 46 cities in the United States and 36 other international destinations. Through commercial agreements with other independent regional carriers, an additional 38 North American communities are served bringing the total network to 188 destinations on five continents.

Air Canada operates an extensive global network in conjunction with its international airline partners. With Air Canada's strategic alliance and commercial partnerships currently in effect, scheduled and charter air transportation is offered to over 800 destinations in more than 130 countries.

Air transportation revenues represent over 91% of consolidated operating revenues. The Corporation also provides aircraft and engine maintenance, ground handling, and other services to airlines and other customers.

a) Principles of Consolidation

The consolidated financial statements are expressed in Canadian dollars and are prepared in accordance with accounting principles generally accepted in Canada. They include the accounts of Air Canada as well as regional airlines Air BC Limited, Air Ontario Inc., Air Nova Inc., and Air Alliance Inc. (until its March 4, 1999 merger with Air Nova), Air Canada Capital Ltd., and a tour operator, Air Canada Vacations (Touram Inc.). They also include the accounts of Canadian Airlines International Ltd. and Canadian Regional Airlines (1998) Ltd. commencing June 30, 2000 (note 2). All of the aforementioned are directly or indirectly wholly-owned subsidiaries of Air Canada.

In February, 2000, 866983 Alberta Limited, doing business as Air Canada Capital Ltd. ("ACC"), was incorporated for the purpose of financing aircraft with Air Canada owning 100% of the common shares. ACC has assumed fifty-eight aircraft leases for which Canadian Airlines International Ltd. ("CAIL") was previously the lessee and has sub-leased these aircraft to CAIL.

Effective January 1, 2001, Air Canada and CAIL were amalgamated and continued as one corporation, with the amalgamated entity being known as Air Canada. Similarly, effective January 1, 2001, Air Canada Regional Inc. (which already operates as Air Nova, Air Ontario and Air Alliance) having acquired the assets and operations of Air Nova and Air Ontario in December, 2000 was amalgamated with Air BC Limited, Canadian Regional Airlines (1998) Ltd. and Canadian Regional Airlines Ltd., with the amalgamated entity being known as Air Canada Regional Inc.

The excess of the acquisition costs of investment in subsidiaries over the Corporation's proportionate share of the underlying value of the net assets at the date of acquisition represents goodwill, and is amortized over periods not exceeding 40 years. Goodwill is reported net of accumulated amortization of $40 (1999 $31). The value of goodwill, and any impairment of that value, is assessed by reference to cash flows.

b) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

c) Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates of exchange in effect at the date of the consolidated statement of financial position. Gains or losses are included in income of the year, except for the gains or losses relating to long-term receivables and debt which are deferred and amortized over the remaining term of the corresponding receivable or debt. Non-monetary assets, liabilities and other items recorded in income arising from transactions denominated in foreign currencies, are translated at rates of exchange in effect at the date of the transaction.

d) Cash and Cash Equivalents

Cash and cash equivalents include short-term investments of $458 (1999 $550). All short-term investments may be liquidated promptly and have maturities of less than ninety days. Reported cash and cash equivalents are netted against outstanding cheques.

e) Spare Parts, Materials and Supplies

Spare parts, materials and supplies are valued at average cost. A provision for the obsolescence of flight equipment spare parts is accumulated over the estimated service lives of the related flight equipment to a 30% residual value.

f) Air Transportation Revenue

Airline passenger and cargo sales are recognized as operating revenues when the transportation is provided. The value of unused transportation is included in current liabilities.

g) Employee Future Benefits

In the first quarter of 2000, the Corporation retroactively adopted with restatement the new Canadian Institute of Chartered Accountants standard #3461 requiring all employee future benefits to be accounted for over the period the service is rendered (note 18). The significant policies adopted under that basis are as follows:

- The cost of pensions and other retirement benefits earned by employees is actuarially determined using the projected benefit method prorated on service, market interest rates, and management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and expected health care costs.
- An adjusted market value method is used to value plan assets for the purpose of calculating the expected return on plan assets. Under this method, realized and unrealized capital gains (losses) arising during a given year are spread on a linear basis over four years.
- Past service costs are amortized linearly over the Expected Average Remaining Service Lifetime (EARSL) of the plan.
- Cumulative unrecognized net actuarial gains and losses in excess of 10% of the greater of the projected benefit obligation or adjusted market value of plan assets are amortized over EARSL.

h) Depreciation and Amortization

Operating property and equipment are depreciated or amortized to estimated residual values based on the straight-line method over their estimated service lives.

	Estimated Residual Values		
	Aircraft	Engines/Rotable Inventory	Period of Amortization
Mainline			
A319-113	15%	15%	20 years
A320-211	15%	15%	20 years
A330-300	n/a	15%	20 years
A340-300	n/a	15%	20 years
Boeing 737-200	15%	15%	20 years
Boeing 747-400	15%	15%	20 years
Boeing 767-200	15%	15%	20 years
Boeing 767-300	15%	15%	20 years
Canadair Regional Jet	15%	10%	20 years
DC-9-32	15%	10%	to December 31, 2006
Regionals			
Various	5-20%	5-20%	4-20 years

Significant aircraft reconfiguration costs are amortized over 3 years. Aircraft introduction costs are amortized over 4 years. Betterments to aircraft on operating leases are amortized over the term of the lease.

i) Maintenance and Repairs

Maintenance and repair costs are charged to operating expenses as incurred. Significant aircraft modification costs are capitalized and amortized over the remaining service lives of the aircraft.

j) Other Operating Expenses

Included in other operating expenses are expenses related to computer network and information technology costs, computer reservation service charges, building rent and maintenance, terminal handling, professional fees and services, crew meals and hotels, advertising and promotion, insurance costs, credit card fees, and other expenses.

k) Loyalty Programs

The incremental cost of providing travel awards for mileage credits earned through air travel under the Corporation's frequent flyer programs is charged to expense when reward levels are reached. In the fourth quarter of 2000, the Corporation retroactively changed, with restatement, its accounting policy related to revenue recognition for the sale of mileage credits to participating non-airline partners. Revenue from the sale of mileage credits to participating non-airline partners, that is estimated to be earned in the future, is deferred and recognized as points are redeemed (note 18).

l) Interest Capitalized

Interest on funds used to finance the acquisition of new flight equipment and other property and equipment is capitalized for periods preceding the dates the assets are available for service.

m) Deferred Credits

Gains on sale and leaseback of assets are deferred and amortized to income over the terms of the leases as a reduction in rental expense.

Contributions received in exchange for extensions to commercial agreements are deferred and amortized to income over the life of the contract extension.

n) Income Tax

In the first quarter of 2000 the Corporation adopted the liability method of accounting for income taxes as required by the new Canadian Institute of Chartered Accountants standard #3465. This standard was applied retroactively, however comparative financial information was not restated (note 18).

For 1999, income taxes were provided for using the deferral method.

o) Financial Instruments

The Corporation manages its foreign exchange exposure through the use of options, forward contracts and cross currency swaps. Resulting gains and losses are accrued as exchange rates change to offset gains and losses resulting from the underlying transactions. Premiums and discounts are amortized over the term of the contracts.

The Corporation also enters into interest rate swap agreements to minimize the impact of changes in rates. Net receipts or payments under the Corporation's swap agreements are accrued as adjustments to interest expense.

The Corporation enters into fuel contracts to manage its exposure to jet fuel price volatility. Resulting gains and losses are recorded as adjustments to fuel expense as fuel is purchased. Premiums and discounts are recorded over the term of the contracts.

p) Route Rights and Slot Purchase Costs

Route rights and slot purchase costs are amortized over 20 years

q) Non-Recurring Labour Expenses

Non-recurring labour expenses in the year 2000 represent one-time costs principally for extending collective agreements and to achieve intermingling of certain Air Canada and Canadian Airlines employee groups related to the acquisition of Canadian Airlines International Ltd.

r) Comparative Figures

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted in the current year.

2. Acquisition of Canadian Airlines International Ltd.

In 1999, 853350 Alberta Ltd. (the "Offeror") was incorporated, with Air Canada owning 10% of the common shares, for the purpose of acquiring the common shares of Canadian Airlines Corporation ("CAC") and the preferred shares of Canadian Airlines International Ltd. ("CAIL").

CAC was a Canadian based holding company which, through its majority-owned subsidiary, CAIL, provided domestic, U.S.-Canada transborder, and international jet air transportation services, and, through an indirect wholly-owned subsidiary of CAIL, Canadian Regional Airlines (1998) Ltd., provided regional jet and turboprop air transportation services

On January 4, 2000, the Offeror took up approximately 82% of the issued and outstanding common shares and non-voting shares of CAC at a cost of $79. On January 5, 2000, the Offeror purchased from a wholly-owned subsidiary of AMR Corporation its investment in convertible preferred shares of CAIL at a cost of $59. At the same time, AMR Corporation relinquished all rights related to its shareholdings in CAIL. Prior to the Offeror taking up the above-mentioned shares of CAC and CAIL, the Competition Bureau of Canada had announced that it would not oppose the acquisition of these shares by the Offeror or Air Canada. Air Canada advanced $138 to the Offeror from its internal funds to provide the financing for these transactions. At the time the offer to acquire the shares of CAC and CAIL was accepted, it was established that CAC was in significant financial difficulty and would require a debt restructuring with its creditors The Offeror then commenced work to assist in a comprehensive restructuring of the debt and obligations of CAC. Air Canada made financing available on acceptable terms during the debt restructuring process. Air Canada entered into an agreement with CAIL's operating bank to increase its operating line of credit by $75.

On March 24, 2000, CAC was granted an order under the Companies' Creditors Arrangement Act (Canada) and an ancillary order under section 304 of the United States Bankruptcy Code. Under the terms of the order, CAC was required to present a plan of arrangement setting out the terms of the restructuring of its debt and other obligations within 30 days of the date of the order.

Following approval by the creditors, the Court of Queen's Bench of Alberta approved the plan on June 27, 2000. The plan resulted in the compromise of the indebtedness owed to secured noteholders and certain affected unsecured creditors of CAC. In connection with the plan, the share capital of CAIL has been reorganized and, as a result, CAIL is now a wholly owned subsidiary of 853350 Alberta Ltd. Air Canada has acquired the remaining 90% of the common shares of 853350 Alberta Ltd. CAC is now a non-operating company without any significant assets. On July 6, 2000, the Toronto Stock Exchange delisted CAC's common shares and non-voting common shares.

Following the approval by the court on June 27, 2000 of the plan of arrangement of CAC, the Corporation assumed control of CAIL for accounting purposes. The acquisition of CAIL has been accounted for using the purchase method of accounting. Therefore, the statement of financial position of CAIL has been consolidated into the Corporation's financial statements as at June 30, 2000. The results of operations of CAIL since the acquisition date have also been included in the Corporation's results.

The following is a summary of the net assets of CAIL acquired as at June 30, 2000 at their estimated fair value.

Assets		
Cash and cash equivalents	$	49
Accounts receivable		450
Spare parts, materials and supplies		101
Prepaid expenses		15
Future income taxes		453
Property and equipment		827
Pension		119
Other assets		98
Goodwill		502
Total Assets	$	2,614
Liabilities		
Accounts payable and accrued liabilities	$	787
Bank indebtedness		110
Restructuring costs		279
Advance ticket sales		364
Current portion of long-term debt and capital lease obligations		65
Long-term debt and capital lease obligations		630
Other long-term liabilities		180
Deferred credits		19
Total Liabilities	$	2,434
Net assets acquired at fair market value for cash consideration	$	180

Included in the above amounts are certain intercompany balances that are eliminated upon consolidation.

The purchase price for CAIL of $180 is offset by $49 of cash acquired from CAIL for a net cash outflow of $131; $6 was disbursed in 1999 and the net cash outflow was $125 in 2000.

Restructuring costs include employee severance ($196), the exit from AMR Systems and Services contract ($79), and other ($4). The Corporation expects employee reductions and the exit from AMR Systems Services contract to be completed in 2001.

Following the process agreed upon with the Canadian Commissioner of Competition pursuant to undertakings entered into by Air Canada in December 1999, Canadian Regional Airlines (1998) Ltd. was offered for sale on June 30, 2000 for a period of sixty days. Since no adequate offer was made during this period, the Corporation has retained and continues to operate this airline.

3. Property and Equipment

	2000	1999
Cost:		
Flight equipment	$ 4,244	$ 3,512
Other property and equipment	1,830	1,603
	6,074	5,115
Accumulated depreciation and amortization:		
Flight equipment	1,423	1,246
Other property and equipment	1,026	904
	2,449	2,150
	3,625	2,965
Progress payments	549	255
Property and equipment at net book value	$ 4,174	$ 3,220

Included in flight equipment are 15 aircraft under capital leases with a cost of $435 less accumulated depreciation of $24 for a net book value of $411.

Interest capitalized during the year amounted to $25 using an average interest rate of 7.60% (1999 $23 at 7.75%).

As at December 31, 2000, flight equipment included six DC-9's, three B747-200's, and one B737 aircraft which are retired from active service with a net book value of $27 which approximates fair market value.

4. Deferred Charges

	2000	1999
Aircraft lease payments in excess of rent expense	$ 1,026	$ 910
Foreign currency exchange on long-term debt	115	174
Financing costs	144	149
Aircraft introduction costs	6	16
Other	28	37
Deferred charges	$ 1,319	$ 1,286

5. Other Assets

	2000	1999
Employer pension plan funding in excess of pension expense	$ 760	$ 580
Security and other deposits	269	164
Notes and other long-term receivables	101	90
Route rights and slot purchase costs net of accumulated amortization of $4 (1999 $1)	94	31
Other	20	7
Other assets	$ 1,244	$ 872

Included in other assets are 384,678 shares in Equant N.V., previously known as SITA Telecommunications Holdings N.V., which are carried at a nominal amount and had a quoted market value of $15 as at December 31, 2000. In 1999, the Corporation sold 60% of its holding for proceeds and a gain of $67 ($46 after tax).

In 2000, the Corporation sold landing slots at Chicago's O'Hare Airport for proceeds and gain of $35 ($24 after tax).

Notes receivable in the amount of $101 bear interest at a weighted average rate of 11.1% and mature 2005 through 2010. The carrying value of notes receivable approximates fair value.

6. Non-Operating Income (Expense)

	2000	1999
Net Interest Expense		
Interest income	$ 51	$ 52
Interest expense	(286)	(229)
Interest capitalized	25	23
Total	(210)	(154)
Amortization of deferred foreign exchange	(24)	(18)
Gain on sale of investments and other assets		
Gain on sale of Equant N.V. shares (note 5)	–	67
Sale of landing slots (note 5)	35	–
Provision for loss on sale of aircraft	(24)	(12)
Other	4	2
Total	15	57
Other		
Gain on purchase of Japanese yen subordinated perpetual debt (note 9)	20	25
Takeover bid defense costs	–	(42)
Financing	(8)	13
Other	(6)	3
Total	6	(1)
Total	$ (213)	$ (116)

7. Long-Term and Subordinated Perpetual Debt and Capital Lease Obligations

	Final Maturity	Interest Rate (%)	2000	1999
U.S. dollar debt (a)	2001-2009	7.0-8.7	$ 1,092	$ 830
Canadian dollar debt (b)	2003-2009	5.8-10.0	1,038	773
Swiss franc debt (c)	2002	5.1	172	169
Deutsche mark debt (d)	2001-2005	6.6-7.1	336	356
Japanese yen notes (e)	2007	5.8	133	161
			2,771	2,289
Convertible subordinated debentures (Note 8)			127	125
Subordinated perpetual debt (Note 9)			840	882
Capital lease obligations (f)	2001-2013	5.2-12.0	402	–
			4,140	3,296
Current portion of long-term debt			(529)	(114)
Long-term and subordinated perpetual debt and capital lease obligations			$ 3,611	$ 3,182

All debt is unsecured by the Corporation with the exception of subsidiaries' debt totalling $113 (1999 $61) which is secured by certain of their assets.

Interest paid on long-term and subordinated debt and capital lease obligations in 2000 was $264 (1999 $266).

Principal repayment requirements for the next five years are as follows:

	2001	2002	2003	2004	2005
Long-Term Debt	$502	$430	$373	$524	$269
Capital Lease Principal Obligations	$27	$30	$86	$77	$26

As at December 31, 2000, the Corporation had a US $370 committed and unsecured revolving credit facility with a group of financial institutions in Canada of which C $520 was drawn. The facility has a maturity ending in 2004 but may be extended by an additional year on each anniversary date. If the facility is not extended, the availability of funds declines until maturity. A portion of the facility was not extended in 1999 with the availability of funds declining to US $308 by 2003. The Corporation also has a C $175 one year committed credit facility with a group of financial institutions in Canada, as well as various other credit lines totalling C $100. A commitment of US $68 has been provided to the Corporation prior to year-end for the sale and leaseback of certain assets at fair market value. This transaction is to be finalized in early 2001.

a) As at December 31, 2000, U.S. dollar debt totalled US $728, of which US $537 is at floating interest rates based on U.S. dollar LIBOR. Approximately 16% of the 2001 interest rate exposure on the floating rate U.S. dollar debt is hedged by short-term interest rate contracts. Of the US $728 debt:
- a US $264 borrowing has a final maturity in 2005 and may be repaid on any interest payment date.
- a US $205 borrowing has a final maturity in 2006 and may be repaid at par in whole or in part on any interest payment date, with an indemnity.
- a US $64 borrowing has a final maturity in 2008 and may be repaid at par in whole or in part any time prior to maturity, with an indemnity.
- a US $195 borrowing has a final maturity in 2009 and may be repaid at par in whole or in part at any time prior to maturity without penalty.

b) Canadian dollar debt is comprised of $230 debentures maturing in 2007, $175 debentures maturing in 2004, $520 drawing on the revolving credit facility, and various other subsidiary debt totalling $113. The debentures are redeemable by the Corporation in whole or in part at any time, with an indemnity.

The following arrangements exist with a credit worthy counterparty related to the debentures above which is comprised of:

i) a swap where the Corporation effectively converted C $230 with a fixed rate of interest into 19,333 Japanese yen with a floating interest rate until maturity in 2007.

ii) a swap where the Corporation effectively converted C $175 with a fixed rate of interest into 12,635 Japanese yen with a floating interest rate until maturity in 2004.

c) Swiss franc debt is comprised of 186 Swiss francs maturing in 2002 that may be called by the Corporation at par on any interest payment date. During 2000 the Corporation purchased foreign exchange contracts that effectively converted 174 Swiss Francs into U.S. dollars and the remaining 12 Swiss francs into Canadian dollars.

d) Deutsche mark debt was D 450 comprised of:
- 250 Deutsche mark bonds maturing in 2001. The Corporation has entered into the following arrangements, with credit worthy counterparties, related to this debt:
  i) effectively converting 125 Deutsche mark 7.1% fixed rate debt into Deutsche mark floating rate debt until May 2001.
  ii) effectively converting 125 Deutsche mark floating rate debt into $102 Canadian floating rate debt until May 2001.
  iii) effectively converting 125 Deutsche mark 7.1% fixed rate debt into $95 Canadian floating rate debt until May 2001.
- 200 Deutsche mark 6.6% fixed rate bonds maturing in 2005. The Corporation has entered into an arrangement, with credit worthy counterparties, related to this debt effectively converting 200 Deutsche mark 6.6% fixed rate debt into $139 Canadian floating rate debt until January 2005.

e) Japanese yen debt is comprised of 10,000 Japanese yen notes. These will be repaid in 14 equal semi-annual instalments ending October 2007. The interest rate on the notes will be reset in 2002 based on interest rate indices. Two thirds of these notes may be called by the Corporation at par on any interest payment date. If the Corporation were to default on its obligations and the debt became payable prior to maturity, one third of the debt amount outstanding under the notes would be payable in U.S. dollars at a predetermined foreign exchange rate.

f) There are a total of 15 aircraft under capital leases with obligations totalling $402 (C $118, US $161, and 2,657 Japanese yen) with interest rates ranging from 5.2-12.0%. Future minimum lease payments are $562, which includes $160 of interest.

8. Convertible Subordinated Debentures

In December 1999, the Corporation issued $150 convertible subordinated debentures which have an annual interest rate of 7.25%, payable quarterly, and are convertible at $16.00 per share, at the holder's option, into Air Canada common shares and Class A non-voting common shares ("Class A shares") at any time up to and including maturity in December 2009. This equals a rate of 6.25 shares per $100.00 principal amount of convertible subordinated debentures.

The Corporation can force conversion into common shares and Class A shares at any time following the seventh anniversary of the issue if the weighted average closing price of the shares of the Corporation for the 20 trading days prior to the date of the redemption provides the holder an internal rate of return of at least 12% for the period commencing from the date of issuance of the convertible subordinated debentures and ending on the redemption date. The internal rate of return calculation includes interest payments made by the Corporation under the convertible subordinated debentures and the excess of the weighted average closing price above $16.00 per share.

$127 of the convertible subordinated debentures, representing the present value of interest and principal payments to December 2009, is classified as long-term debt. An amount of $25, representing the value of the conversion option, is classified as share capital. Over the life of this instrument, the $127 will be increased to $150 to provide an annual interest expense equal to the then market interest rate of similar debt instruments of 10%.

These debentures rank subordinate to all obligations and debt which are not subordinated according to their terms.

9. Subordinated Perpetual Debt

	2000	1999
49,000 (1999 54,000) Japanese yen at 2.60% until 2004 Callable in 2004 and every fifth year thereafter at par (a)	$ 643	$ 763
300 Swiss francs at 6.25% Callable in 2001 and every fifth year thereafter at 102% of par	278	272
200 Swiss francs at 5.75% Callable at 102% of par in 2004 and every fifth year thereafter at 102% of par	185	181
200 Deutsche marks at 5.500% Callable in March 2003 and every third year thereafter at par (b)	144	149
Subordinated perpetual debt, at year-end foreign exchange rates	1,250	1,365
Less foreign exchange	(410)	(483)
Subordinated perpetual debt	**$ 840**	**$ 882**

The maturity of this subordinated perpetual debt is only upon the liquidation, if ever, of the Corporation. Principal and interest payments on the debt are unsecured and are subordinated to the prior payment in full of all indebtedness for borrowed money. The effects of foreign exchange fluctuations on the principal amount since the issuance of the debt have not been recorded since it is not probable that circumstances will arise requiring redemption of the debt and since, under present circumstances, it is not probable that the Corporation will call the debt. As at December 31, 2000 the foreign exchange fluctuation related to 49,000 Japanese yen is $236 (1999 $315 for 54,000 Japanese yen), 500 Swiss francs is $127 (1999 $117), and 200 Deutsche marks is $47 (1999 $51).

a) The interest rate on the yen subordinated perpetual debt is 2.60% until 2004 and will be reset for each subsequent five-year reset period based upon a capped spread over the Japanese long-term prime lending rate. In 2000, through a subscription arrangement with a major financial institution, the Corporation purchased from certain syndicate loan members their rights to 5,000 Japanese yen in this borrowing. Together with 1999 purchases, the Corporation now holds the rights to 11,000 Japanese yen in this borrowing. The Corporation has entered into an interest rate swap effectively fixing the next interest rate reset for 10 per cent of the outstanding principal at interest rates similar to that currently being paid.

b) The interest rate on the Deutsche mark subordinated perpetual bonds is 5.5% until March, 2003 and will be reset for each subsequent three-year reset period based upon an interest rate index.

10. Deferred Credits

	2000	1999
Gain on sale and leaseback of assets	$ 350	$ 255
Aircraft rent expense in excess of lease payments	337	288
Contributions received in exchange for extensions of commercial agreements (note 1m)	286	297
Other	11	18
Deferred credits	$ 984	$ 858

In 1999, in exchange for extensions of commercial agreements with Star Alliance partners United Airlines and Deutsche Lufthansa and an Aeroplan partner, Canadian Imperial Bank of Commerce, the Corporation recorded contributions of $108 and $190 respectively (note 11).

11. Share Capital

The authorized capital of the Corporation consists of an unlimited number of common shares, Class A non-voting common shares ("Class A shares"), Class A preferred shares issuable in series and Class B preferred shares issuable in series. The Corporation's Articles of Amalgamation under provisions of the Canada Business Corporations Act include limits on individual and aggregate non-resident public ownership of common shares of 10 per cent and 25 per cent respectively, including associates of such shareholders. Under Bill C-26 which came into effect on June 29, 2000, the maximum individual holding threshold provided for in the Air Canada Public Participation Act has been increased from 10% to 15%. Accordingly, an amendment to the articles to reflect this legislative change will be proposed to the shareholders at the annual and special meeting on May 15, 2001.

In 1993, the Corporation issued 21,750,000 common share purchase warrants valued at $1.00 each. Each warrant entitled the holder to purchase one common share at $6.25. 21,741,950 of these common share purchase warrants had not been exercised and expired. The remaining value of $22 was removed from share capital in 1999 and the after tax amount of $15 was credited to contributed surplus.

In 1999, the Corporation undertook several share capital initiatives as follows:

a) In December 1999, the Corporation bought back and cancelled 41,668,630 common shares and 27,079,856 Class A shares for $16.00 each or $1,100 in total. The net book value per share amounts of these shares of $6.68 and $7.06 respectively or $470 in aggregate, was charged to share capital and the remaining $630 was charged to retained earnings.

b) In December 1999, the Corporation issued 10 million Class A Convertible Participating Non-Voting Preferred Shares, Series 1 ("Series 1 Preferred Shares") to Expo Investment Partnership, L.P., a partnership formed by UAL Corporation and Deutsche Lufthansa AG, two of Air Canada's Star Alliance partners, for a cash consideration of $233 of which $125 represented the fair market value of the shares and $108 represented a contribution to extend the Star Alliance agreement (note 10). These shares are entitled to receive dividends equal to the amount paid to holders of the Corporation's common shares. The shares are not redeemable by the Corporation prior to December 31, 2009 unless either of the partners ceases to be a participant in the Star Alliance and as a result the Corporation terminates its Alliance Agreement or either partner is in breach of any Alliance Agreement which leads to the Corporation terminating its Alliance Agreement. On or after December 31, 2009, the Corporation may redeem the shares for $25.00 per share plus declared and unpaid dividends and a gross-up for dividends and deemed dividends. These shares contain certain covenants, including covenants that prohibit the Corporation from i) entering into certain strategic alliances and similar arrangements with other airlines (other than existing alliance arrangements); ii) violating its existing Alliance Agreements with UAL Corporation and Deutsche Lufthansa AG if the violation could reasonably be expected to have a material adverse impact on the revenues which members of the Star Alliance would derive from the Alliance Agreements (a "Material Star Impact"); iii) selling any slots, planes, routes, gates or any interests in commuter airlines if the transaction could be reasonably expected to have a Material Star Impact and iv) declaring or paying dividends or other distributions, other than stock dividends, if, after such payment, the Corporation's shareholders' equity would be less than $1,250. UAL and Lufthansa have agreed with Air Canada that covenants i) to iii) above will be null and void upon UAL, Lufthansa and Air Canada agreeing on binding terms applicable to all Star Alliance members (through charter provisions, alliance agreements or otherwise) which would solidify a close and binding commitment of such members to the Star Alliance. The Corporation is currently in the process of concluding an agreement on the above referenced binding terms. If such binding terms have not been agreed by September 30, 2001, UAL has agreed to issue to Air Canada preferred shares in its capital stock containing covenants substantially similar to covenants i) to iii) above, failing which such covenants will terminate on October 1, 2001. The holder of the Preferred Shares has the option to redeem the Preferred Shares at $25.00 per Share (plus a premium of 1% in the event there is a change of control of the Corporation and a gross-up for dividends and deemed dividends) if: the Corporation breaches an Alliance Agreement in a manner which does or could reasonably be expected to have a Material Star Impact; a breach of certain covenants occurs; a change of control of the Corporation occurs that does or is reasonably expected to have a Material Star Impact; or the Corporation refuses to extend the Alliance Agreements after they expire at any time on or after December 31, 2009. The holder may convert each preferred share at any time into a) 1.0417 non-voting common shares for $24.00 or b) an equal number of Class A Convertible Participating Non-Voting Preferred Shares, Series 2, which are transferable to third parties but do not contain certain of the covenants described above. The holder is entitled to receive, in priority to common and Class A non-voting shares, $25.00 per share plus any declared and unpaid dividends in the event of liquidation of the Corporation. In the event the Corporation breaches its obligations under the Alliance Agreements in a manner material and adverse to the revenues of UAL or Lufthansa and the Alliance Agreements are terminated, the Corporation has agreed to pay liquidated damages in amounts declining over a ten year period from $250 to $37.

c) In October 1999, the Corporation received a cash consideration of $200 from the Canadian Imperial Bank of Commerce of which $190 was applied to the extension of their Aeroplan commercial agreement to December 31, 2009 (note 10) and an ascribed value of $10 was applied to the issuance of 4.7 million warrants. The warrants will expire in October, 2004 and will each be convertible to one Class A share at $24.00.

The takeover bid related transactions described above and the convertible subordinated debenture transaction described in note 8 affect various earnings per share calculations. Earnings per share values for 1999 and 2000 have been based upon time-weighted average number of outstanding basic and fully diluted shares. For the year ended December 31, 2000, the time-weighted average number of outstanding shares was 120.1 million basic and on a fully diluted basis, 150.7 million shares. At December 31, 2000, there were 120.2 million basic shares outstanding and, on a fully diluted basis, there would have been 150.8 million shares.

The issued capital consists of common shares, Class A shares and Class A Convertible Participating Non-Voting Preferred Shares, Series 1 ("Series 1 Preferred Shares"). The changes during 1999 and 2000 in the outstanding number of common and Class A shares and their aggregate stated value during those years are as follows:

	Common Shares		Class A Shares	
	Number	Amount	Number	Amount
December 31, 1998	120,222,818	$ 819	67,913,728	$ 486
Share purchase options exercised	184,025	1	250,188	1
Expired warrants	–	(22)	–	–
Shares cancelled through buy-back	(41,668,630)	(279)	(27,079,856)	(191)
December 31, 1999	78,738,213	519	41,084,060	296
Share purchase options exercised	312,680	2	25,366	[illegible]
December 31, 2000	79,050,893	$ 521	41,109,426	$ 296

	2000	1999
Share Capital Summary (net of issue costs):		
Common shares	$ 521	$ 519
Class A shares	296	296
Class A non-voting preferred shares	125	125
Warrants	10	10
Convertible subordinated debenture conversion option	25	25
Total	$ 977	$ 975

Stock Option Plan

The details of the Corporation's share option plan, under which eligible employees are granted options to purchase common shares and Class A shares, at a price not less than the market value of the shares at the date of granting, are as follows:

	Total Outstanding	Weighted Average Remaining Contractual Life (Years)	Range of Exercise Price	Outstanding Weighted Average Exercise Price	Total Exercisable	Exercisable Average Exercise Price
Common	292,932	8.42 years	$5.00 – $6.99	$ 6.63	76,403	$ 6.57
	2,491,745	8.21	$9.00 – $13.99	$ 10.38	497,657	$ 11.41
	1,317,317	8.18	$14.00 – $15.99	$ 14.90	335,734	$ 14.68
	828,973	8.05	$16.00 – $19.99	$ 16.20	223,321	$ 16.23
	4,930,967				1,133,115	
Class A Non-Voting	344,180	7.14	$4.00 – $5.99	$ 5.09	176,320	$ 4.62
	138,841	8.13	$6.00 – $9.99	$ 8.90	22,529	$ 6.00
	215,002	7.12	$10.00 – $13.99	$ 12.95	107,501	$ 12.95
	560,299	6.91	$14.00 – $17.99	$ 15.14	284,160	$ 14.90
	1,258,322				590,510	

A summary of recent option activities is as follows:

	2000 Shares (000)	2000 Weighted – average exercise price	1999 Shares (000)	1999 Weighted – average exercise price
Common shares				
Beginning of year	2,905	$ 9.43	1,437	$ 12.85
Granted	2,346	11.17	1,767	8.79
Exercised	(313)	16.31	(191)	9.90
Forfeited	(10)	8.86	(108)	8.43
End of year	4,931	12.34	2,905	9.43
Class A shares				
Beginning of year	1,168	$ 8.17	825	$ 10.51
Granted	116	9.34	601	6.35
Exercised	(25)	15.18	(251)	9.30
Forfeited	(1)	4.17	(7)	9.47
End of year	1,258	11.33	1,168	8.17

All options are exercisable on the basis of 25% of the options per year on a cumulative basis, beginning after one year and expiring after ten years.

Proceeds from the exercising of share options are applied to the applicable share capital account upon receipt.

Shareholder Rights Plan

The Corporation's Board of Directors approved a shareholders' rights plan, effective March 15, 2000, which was ratified at the 2000 annual shareholders meeting. This "Rights Plan" is intended to ensure, to the extent possible, that all shareholders are treated equally and fairly in connection with any takeover offer for Air Canada. The term of the Rights Plan is until the date of the 2002 annual shareholders meeting. Under the Rights Plan, one right will be issued for each common share and class A share outstanding. The rights initially entitle holders to acquire additional common or class A shares, as the case may be, at a price of $100.00 per share. However, following certain acquisition events, each right will entitle the holder thereof (other than the acquiring person or group) to purchase shares having a fair market value of $200.00 for $100.00.

Share Appreciation Plans

The Corporation has the following two share appreciation plans:

1) **Pilots:** This plan was entered into in September 1998 and involved the immediate issuance of 2 million units with an additional 1 million units issued in March 2000, in both cases exercisable unconditionally six months later. An additional 1 million units will be issued in March 2001 and exercisable six months later, conditional on the Corporation achieving certain operating margins. The redemption value of each unit is for the difference between $7.50 and the market value of the Corporation's common shares at the time of redemption. These units can be redeemed up until September 2003. The cumulative liability for these units is deferred and amortized to expense over the life of the agreement. The expense for this program in 2000 was $1. In the year, 703,757 units were redeemed.

2) **Management and Administrative and Technical Support group:** This plan was entered into in February 1999 and involved the issuance of 1 million units in March 1999 with an additional 0.5 million issued in March 2000, in both cases exercisable unconditionally in six months. An additional 0.5 million units will be issued in March 2001 and exercisable six months later conditional on the Corporation achieving certain operating margins. The redemption value of each unit is for the difference between $6.09 and the market value of the Corporation's common shares at the time of redemption. These units can be redeemed up until September 2004. The cumulative liability for these units is deferred and amortized to expense over the period leading up to the first possible date of redemption and any subsequent change in the liability is fully expensed on a monthly basis thereafter. The expense for this program in 2000 was $8. In the year, 357,034 units were redeemed.

12. Future Income Taxes

Effective January 1, 2000, the Corporation changed its method of accounting for income taxes from the deferral method to the liability method as required by the new Canadian Institute of Chartered Accountants standard #3465. The liability method requires that accumulated tax balances be adjusted to reflect changes in the tax rates. This standard was applied retroactively, however as permitted under the new rules, comparative financial information has not been restated.

The cumulative effect of this change as of January 1, 2000 was a reduction in future income taxes of $36, offset by a credit to opening retained earnings (deficit).

Future income taxes reflect the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Corporation's future tax assets and liabilities as of December 31, 2000 are as follows:

Future tax assets:	
Non-capital loss carry forwards	$ 310
Loyalty program deferred revenue	219
Deferred gains on sale and leaseback of assets	130
Advance ticket sales	108
Restructuring provision	127
Other	300
Total future tax assets	1,194
Future tax liabilities:	
Tax depreciation in excess of book depreciation	405
Post-employment obligations	20
Other	169
Total future tax liabilities	594
Net future tax assets	$ 600

The reconciliation of income tax attributable to continuing operations, computed at the statutory tax rates, to income tax expense is as follows:

	Liability Method 2000	Deferral Method 1999
Provision (recovery) based on combined federal and provincial tax rates	$ (52)	$ 110
Non-taxable portion of capital gains	(15)	(8)
Large corporations tax	7	7
Non-deductible expenses	19	17
Change in future income taxes resulting from tax rate reductions	1	–
Other	(5)	(5)
Provision for (recovery of) income taxes	$ (45)	$ 121

Significant components of the provision for (recovery of) income taxes attributable to continuing operations are as follows:

	Liability Method 2000	Deferral Method 1999
Current tax expense (recovery)	$ (3)	$ 18
Future income tax expense (benefit) relating to temporary differences	(43)	113
Future income tax expense (benefit) from recognition of loss carry forwards	–	(10)
Future income tax expense (benefit) from tax rate reductions	1	–
Income tax expense (recovery)	$ (45)	$ 121

The following are the tax loss expiry dates for which the tax benefits have been recognized in the financial statements:

Year of Loss	Year of Expiry	Tax Losses
1995	2002	$ 168
1996	2003	23
1997	2004	129
1998	2005	172
1999	2006	282
2000	2007	2
		$ 776

Income taxes paid in 2000 were $26 (1999 $8).

13. Commitments

The Corporation has commitments to purchase, along with spare engines, four Airbus A330-300 and five Airbus A321 in 2001, seven Airbus A321, five Airbus A319 and two Airbus A340-500 in 2002 and three Airbus A340-500 and two Airbus A319 in 2003. Payments under the commitments of US $1,370 are payable as follows:

	US
2001	$ 511
2002	552
2003	307

The Corporation has received financing commitments for 100% of two of the Airbus A330 aircraft, and for a number of Airbus A319 and A321 aircraft not to exceed US $384, as well as up to 85% of the other aircraft purchases. The Corporation has entered into certain interest rate swaps in 2000 with a credit worthy counterparty in support of the anticipated financing of four Airbus A330 aircraft in 2001. The fair value of these interest rate swaps at December 31, 2000 was $16 in favour of the counterparty (1999 $0).

The Corporation has also committed to leasing, under operating leases, aircraft on a long term basis to be delivered as follows: four Boeing 767-300 and three Airbus A319 in 2001, three Airbus A319 and three Airbus A320 in 2002. The total lease payments over the full term of the leases will be approximately US $780. The Corporation has entered into certain interest rate swaps in 2000 with a credit worthy counterparty in support of the leasing of two Boeing 767-300 aircraft in 2001. The fair value of these interest rate swaps at December 31, 2000 was $9 in favour of the counterparty (1999 $0).

Other commitments in 2001 and 2002 for property, ground equipment and spare parts, amount to approximately $146.

Future minimum lease payments under existing operating leases of aircraft and other property total $5,761 and are payable as follows:

	Operating Leases of Aircraft	Operating Leases of Other Property
2001	$ 964	$ 105
2002	882	93
2003	852	85
2004	750	75
2005	584	66
Remaining years	961	344
	$ 4,993	$ 768

Operating lease commitments include currency swaps to convert a significant portion of U.S. dollar lease rentals into Canadian dollar lease rentals for five Canadair Regional Jet operating leases until lease terminations in 2007 and to convert a significant portion of Canadian dollar lease rentals into U.S. dollar lease rentals for three Airbus A330 operating leases until January, 2010. These currency swaps, with credit worthy counterparties, were put in place at the time the leases were concluded and have a fair value at December 31, 2000 of $5 (1999 $5) in favour of the counterparties taking into account foreign exchange rates in effect at that time.

14. Pension Plan and Other Benefit Plans

The Corporation and its subsidiaries maintain several defined benefit plans providing pension, other retirement and post-employment benefits to its employees.

Information about the Corporation's defined benefit plans, in aggregate, is as follows:

	Pension Benefits		Other Benefits	
	2000	1999	2000	1999
Change in benefit obligation				
Benefit obligation at beginning of year	$ 5,214	$ 5,331	$ 348	$ 333
Acquisition	2,138	–	34	–
Service cost	127	97	26	10
Interest cost	460	315	27	22
Plan participants' contributions	90	64	–	–
Amendments	213	401	2	–
Benefits Paid	(297)	(253)	(33)	(16)
Actuarial (gain) loss	535	(717)	72	–
Foreign exchange	(1)	(24)	3	(1)
Benefit obligation at end of year	8,479	5,214	479	348
Change in plan assets				
Fair value of plan assets at beginning of year	6,288	5,474	32	32
Acquisition	2,257	–	2	–
Actual return on plan assets	705	939	4	5
Employer contribution	60	107	28	11
Plan participants' contributions	90	64	–	–
Benefits paid	(297)	(253)	(33)	(16)
Foreign exchange	(2)	(43)	–	–
Fair value of plan assets at end of year	9,101	6,288	33	32
Funded status	622	1,074	(446)	(316)
Unrecognized net actuarial (gain) loss	(930)	(1,309)	32	(40)
Unrecognized prior service cost	887	759	29	32
Unrecognized net transition obligation	(69)	(91)	–	–
Valuation allowance	(23)	–	–	–
Prepaid (accrued) benefit cost	$ 487	$ 433	$ (385)	$ (324)
Weighted average assumptions as of December 31				
Discount rate	6.75%	7.25%	6.75%	7.25%
Expected return on plan assets	8.00%	8.00%	8.00%	8.00%
Rate of compensation increase	4.50%	4.50%		

For measurement purposes, a 14% increase in drug costs was assumed for 2000, decreasing to an ultimate rate of 5.5% in 2006. A 7.5% increase in hospital and other costs was assumed for 2000, decreasing to an ultimate rate of 5.5% in 2004.

Following court approval on June 27, 2000, the Corporation assumed control of Canadian Airlines International Ltd. As a result, the pension benefit obligation was increased by $2,138 and pension plan assets by $2,257. Other employee future benefit obligations were increased by $34 and plan assets by $2.

Included in the above accrued benefit obligation and fair value of plan assets at December 31 are the following amounts in respect of plans that are not fully funded:

	Pension Benefits Plans		Other Benefit Plans	
	2000	1999	2000	1999
Accrued benefit obligation	$ 1,572	$ 246	$ 479	$ 348
Fair value of plan assets	1,090	–	33	32
Funded status	$ (482)	$ (246)	$ (446)	$ (316)

The Corporation's net benefit plan expense is as follows:

	Pension Benefits Plans		Other Benefit Plans	
	2000	1999	2000	1999
Net benefit plan expense				
Current service cost	$ 127	$ 97	$ 26	$ 10
Interest cost	460	315	27	22
Expected return on plan assets	(524)	(382)	(2)	–
Amortization of prior service cost	87	37	5	5
Amortization of net transition obligation	(22)	(22)	–	–
Amortization of experience (gains) losses	3	8	(2)	–
	$ 131	$ 53	$ 54	$ 37

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A 1% change in assumed health care cost trend rates would have the following effects:

	1% Increase	1% Decrease
Effect on total of service and interest cost components	$ 2	$ (2)
Effect on post-retirement benefit obligation	$ 21	$ (23)

15. Financial Instruments and Risk Management

The Corporation manages its exposure to changes in interest rates, foreign exchange rates and jet fuel prices through the use of various derivative financial instruments. Senior management is responsible for setting acceptable levels of risk and reviewing risk management activities as necessary. The Corporation uses derivative financial instruments only for the purpose of hedging existing commitments or obligations, not for generating trading profits.

Credit Exposure of Derivatives

The Corporation's theoretical risk in the derivative financial instruments described below is the cost of replacing the contracts at current market rates in the event of default by any of the counterparties. However, the Corporation does not anticipate such default as it only transacts with credit worthy counterparties, and the relative market positions with each counterparty are monitored to ensure an adequate diversification of risk.

Interest Rate Risk Management

The Corporation has entered into interest rate swap agreements in order to manage the interest rate exposure associated with certain long-term debt obligations. The notional amounts of the swaps do not represent amounts exchanged between parties and are not a measure of the Corporation's exposure resulting from the use of swaps. The amounts exchanged are based on interest rates applied to the notional amounts. The fair value of interest rate swap agreements as at December 31, 2000 was $2 (1999 $17) in favour of counterparties, taking into account interest rates in effect at that time.

The Corporation has also entered into various forward interest rate agreements to manage the risks associated with interest rate movement on the short-term investment portfolio and U.S. and Canadian floating rate debt. The notional amounts of the agreements do not represent amounts exchanged between parties and are not a measure of the Corporation's exposure resulting from the use of the agreements. The amounts exchanged are based on interest rates applied to the notional amounts. The aggregate fair value of contracts outstanding at December 31, 2000 was $1 in favour of the counterparties (1999 $0).

Foreign Exchange Risk Management

The Corporation has entered into certain foreign exchange contracts to manage risks associated with foreign currency exchange rates. As at December 31, 2000 the aggregate face amount of such contracts was approximately $181 (1999 $294). The related fair market value of these contracts at December 31, 2000 was $8 (1999 not material) in favour of the Corporation. In 2000 the Corporation entered into foreign exchange forward contracts effectively converting 186 Swiss Franc long-term debt to U.S. and Canadian dollars (note 7). As at December 31, 2000 the fair market value of these contracts was $16 in favour of the Corporation.

The Corporation has also entered into cross currency swap agreements. The fair value of these agreements at December 31, 2000 was $15 (1999 $3) in favour of the Corporation and $52 (1999 $88) in favour of counterparties.

Fuel Price Risk Management

The Corporation enters into contracts with certain financial intermediaries, not exceeding two years, to manage its exposure to jet fuel price volatility. Gains and losses resulting from fuel hedging transactions are recognized as a component of fuel expense. As at December 31, 2000 the Corporation had effectively hedged approximately 26% of its projected 2001 fuel requirements. As at December 31, 2000 the fair value of fuel contracts was $25 in favour of the counterparties (1999 $36 in favour of the Corporation).

Concentration of Credit Risk

The Corporation does not believe it is subject to any significant concentration of credit risk. Cash and short-term investments are in place with major financial institutions, Canadian governments and major corporations. Accounts receivable are generally the result of sales of tickets to individuals through geographically dispersed travel agents, corporate outlets, or other airlines, often through the use of major credit cards.

Statement of Financial Position Financial Instruments – Fair Values

The carrying amounts reported in the consolidated statement of financial position for cash and short-term investments, accounts receivable and accounts payable approximate fair values due to the immediate or short-term maturities of these financial instruments.

The fair value of long-term debt, including the current portion, is based on rates currently available to the Corporation for debt with similar terms and maturities. The fair value of subordinated perpetual debt is calculated assuming the debt has no maturity date and using an estimated rate based on current interest rates. Management believes at the present time there is very little market for new perpetual debt issues and the fair value of the perpetual debt as calculated does not reflect any premium or discount that may be realized if the perpetual debt was traded in an open market. The fair value of long-term and subordinated perpetual debt and capital lease obligations as at December 31, 2000 was $4,260 (1999 $3,480) compared with carrying values, net of deferred foreign currency exchange, of $4,024 (1999 $3,122). The Corporation also has interest rate swaps related to aircraft financing commitments (note 13).

16. Contingencies

Various lawsuits and claims are pending by and against the Corporation and provisions have been included in current liabilities where appropriate. It is the opinion of management supported by counsel that final determination of these claims will not have a material adverse effect on the financial position or the results of the Corporation.

Under certain aircraft lease agreements, the Corporation may be required to provide residual value support not exceeding $539. Independent appraisals as at December 31, 2000 have indicated it is unlikely the Corporation will be required to provide this support beyond amounts for which provisions are being reflected in the Corporation's accounts. The Corporation retains a residual value interest in these leased aircraft through purchase options.

In 1989, the Corporation concluded an agreement with a substantial financial institution where, upon payment by the Corporation, the financial institution assumed liability for scheduled payments relating to a long-term obligation in an amount of $64 and interest thereon. This obligation which amounts to $43 at December 31, 2000 is extinguished for financial reporting purposes and has been removed from the Corporation's statement of financial position. Until the assumed liability has been fully discharged by the financial institution, the Corporation remains contingently liable for such obligation in the remote event that the counterparty fails to perform.

17. Segment Information

The Corporation operates in one business segment, air transportation and related services. The services within that segment are as follows:

		2000	1999
Transportation Revenue:			
Domestic Air Canada/CAIL:	Passenger	$ 2,714	$ 1,953
	Cargo	127	95
Regional Airlines (AC/CRAL):	Passenger	794	557
	Cargo	19	14
		3,654	2,619
Canada-U.S. Transborder Air Canada/CAIL:	Passenger	2,039	1,518
	Cargo	37	35
Regional Airlines (AC/CRAL):	Passenger	206	153
	Cargo	2	1
		2,284	1,707
Other International Air Canada/CAIL:	Passenger	2,196	1,339
	Cargo	357	242
		2,553	1,581
Total transportation revenue		8,491	5,907
Non-transportation revenue		792	536
Total revenues		$ 9,283	$ 6,443

For passenger and cargo, the allocation to service is determined based on flight destination. Non-transportation revenues are almost exclusively attributable to Canada. Revenues for Canadian Airlines International Ltd. (CAIL) and Canadian Regional Airlines (1998) Ltd. (CRAL) have been included in the actual reported results commencing July 1, 2000.

Property and Equipment:

Air Canada is a Canadian based domestic and international carrier and while the Corporation's flight equipment is used on various routes internationally, for purposes of segment reporting, the Corporation attributes the location of flight equipment to Canada. As a consequence, substantially all of the Corporation's property and equipment is related to operations in Canada.

18. Accounting Standard Changes

During 2000, the Corporation adopted changes in accounting policies in the following areas:

- Employee Future Benefits
- Future Income Taxes
- Loyalty Programs

Employee Future Benefits

In the first quarter 2000, the Corporation adopted retroactively, with restatement of prior periods, the new Canadian Institute of Chartered Accountants standard #3461 – Employee Future Benefits (CICA #3461). The standard requires that all employee future benefits be accounted for over the period the service is rendered.

CICA #3461 was applied in a manner that produced recognized and unrecognized amounts for employee future benefit plans the same as those determined by the application of generally accepted accounting principles in the United States as previously reported by the Corporation in its annual report. The impact of the application of CICA #3461 was the recognition of a net other long term liability of $314 as at January 1, 1999 and a reduction to opening 1999 retained earnings on an after tax basis in the amount of $182. As a result of this change, operating expenses for the year 2000 have increased by an estimated $62 ($37 after tax) (1999 increase of $62; $36 after tax).

Future Income Taxes

In the first quarter 2000, the Corporation adopted retroactively the new Canadian Institute of Chartered Accountants standard #3465 – Income Taxes (CICA #3465), which requires the adoption of the liability method rather than the deferral method of accounting for income taxes wherein accumulated tax balances are adjusted to reflect changes in tax rates. Previous year figures have not been restated to reflect the change for CICA #3465.

The impact of the application of CICA #3465 was a reduction in future income taxes of $36 as at January 1, 2000 offset by a credit to retained earnings. The provision for income tax for the period was not materially affected by this change.

Loyalty Programs

The U.S. Securities and Exchange Commission issued Staff Accounting Bulletin 101 (SAB 101), Revenue Recognition in Financial Statements. SAB 101 provides guidance on conditions that must be met before revenue may be recognized. The Ontario Securities Commission (OSC) stated that this guidance should also be applied to reporting issuers in Ontario. As a result, in the fourth quarter 2000, the Corporation adopted retroactively, with restatement of prior periods, a change in its method of revenue recognition for the sale of mileage credits to third parties in its loyalty program. The proceeds from the sale of mileage credits which represent the Corporation's estimated obligation to provide future travel will be deferred and recognized as points are redeemed. The impact of this change in accounting policy defers to future periods previously recognized revenues. This change does not impact the current method of accounting for mileage credits earned through air travel under the Corporation's frequent flyer programs.

The impact of the application of SAB 101 was the recognition of a liability as at January 1, 1999 of $185 and a reduction to opening 1999 retained earnings on an after tax basis in the amount of $107. As a result of the change, 2000 other revenues were adversely impacted by $12 and other expenses were favorably impacted by $2, for an operating income reduction of $10 ($6 after tax). 1999 other revenues have been reduced by $66 and other expenses $2 for an operating income reduction of $64 ($40 after tax).

The impact on Canadian Airlines' frequent flyer program, Canadian Plus, was an increase of $164 to the liability offset by an after tax charge of $92 to goodwill as at the date of acquisition. As a result of the change, 2000 other revenue was adversely impacted by $9 and other expenses were adversely impacted by $6 for an operating income decrease of $15 ($9 after tax).

Summary of adjustments to retained earnings related to accounting changes:

	2000	1999
Retained earnings (deficit) beginning of year as originally reported	$ (265)	$ 152
Employee future benefits	(218)	(182)
Income taxes	36	–
Loyalty programs	(147)	(107)
Adjustments relating to changes in generally accepted accounting principles	(329)	(289)
Deficit, beginning of year as restated	$ (594)	$ (137)

19. United States Generally Accepted Accounting Principles

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada (Canadian GAAP) which differ in certain respects from accounting principles generally accepted in the United States (US GAAP). The following represents the principle differences affecting net income and shareholders' equity. It does not include all the disclosures required by US GAAP.

	2000	1999
Consolidated Statement of Operations		
Income (loss) for the year in accordance with Canadian GAAP	$ (82)	$ 140
Convertible debentures [1]	2	–
Unrealized foreign exchange gain (loss) on translation of:		
Long-term debt with principal repayment requirements [2]	59	114
Subordinated perpetual debt [3]	73	140
Employee severance costs [4]	(46)	–
Goodwill amortization adjustment [4][8]	(2)	–
Aircraft introduction costs [5]	10	(16)
Revenue recognition adjustment [6]	(249)	64
Current year income adjustments before the following	(153)	302
Income tax recovery (provision) [7]	122	(74)
CAIL equity accounting adjustment [8]	(124)	–
Current year income adjustments	(155)	228
Income (loss) for the year in accordance with US GAAP [9]	(237)	368
Minimum pension liability adjustment net of tax of $3 (1999 $17) [10]	(6)	21
Unrealized gain (loss) on available-for-sale securities net of tax of $16 (1999 $21) [11]	(36)	46
Comprehensive income (loss) for the year in accordance with US GAAP [12]	$ (279)	$ 435
Consolidated Statement of Financial Position		
Future income taxes		
Balance under Canadian GAAP	$ 239	$ 125
Revenue recognition adjustment [6]	–	(105)
Future income taxes [7]	117	142
Balance under US GAAP	$ 356	$ 162

	2000	1999
Deferred charges		
Balance under Canadian GAAP	$ 1,319	$ 1,286
Adjustment for foreign currency exchange on long-term debt (2)	(115)	(174)
Aircraft introduction costs (5)	(6)	(16)
Balance under US GAAP	$ 1,198	$ 1,096
Goodwill		
Balance under Canadian GAAP	$ 527	$ 35
Employee severance costs [4]	(100)	–
Amortization adjustment [4][8]	(2)	–
CAIL equity accounting adjustment [8]	(124)	–
Balance under US GAAP	$ 301	$ 35
Other assets:		
Balance under Canadian GAAP	$ 1,244	$ 872
Adjustment for pension costs [10]	122	61
Available-for-sale securities [11]	15	67
Balance under US GAAP	$ 1,381	$ 1,000
Accounts payable and accrued liabilities		
Balance under Canadian GAAP	$ 2,269	$ 1,045
Employee severance costs [4]	(127)	–
Revenue recognition adjustment [6]	–	(83)
Balance under US GAAP	$ 2,142	$ 962
Long-term and subordinated perpetual debt:		
Balance under Canadian GAAP	$ 3,611	$ 3,182
Reclassification of convertible debentures [1]	23	25
Foreign exchange on subordinated perpetual debt [3]	410	483
Balance under US GAAP	$ 4,044	$ 3,690
Other long-term liabilities		
Balance under Canadian GAAP	$ 1,175	$ 807
Revenue recognition adjustment [6]	–	(166)
Post-retirement benefit costs other than pension [10]	–	(19)
Adjustment for pension costs [10]	133	63
Balance under US GAAP	$ 1,308	$ 685
Shareholders' equity (deficiency):		
Balance under Canadian GAAP	$ 316	$ 363
Reclassification of convertible debentures	(25)	(25)
Current year income adjustments	(155)	228
Current year adjustments for comprehensive income:		
Pension costs	(6)	21
Available-for-sale securities	(36)	46
Cumulative prior year adjustments for:		
Foreign currency exchange:		
Subordinated perpetual debt	(483)	(623)
Long-term debt	(174)	(288)
Revenue recognition adjustment	147	107
Pension costs	–	(2)
Post-retirement benefit costs other than pension	–	10
Aircraft introductory costs	(16)	–
Future income tax	151	236
Comprehensive income – pension costs	(2)	(38)
– available-for-sale securities	67	–
Balance under US GAAP	$ (216)	$ 35

(1) Under Canadian GAAP, proceeds from the issue of convertible securities are split between long-term debt and shareholders' equity, resulting in a debt discount that is amortized to expense over the term of the debt. Under US GAAP, convertible securities are treated as long-term debt in their entirety.

(2) Under Canadian GAAP, unrealized exchange gains and losses arising on the translation of long-term debt repayable in a foreign currency are deferred and amortized to income over the remaining life of the related debt. Under US GAAP, such exchange gains and losses are included in income in the period in which occurred.

(3) Under Canadian GAAP, unrealized gains and losses pertaining to subordinated perpetual debt repayable in a foreign currency are not required to be recognized in income in the period that they arise. Under US GAAP, such exchange gains and losses are included in income in the period in which occurred.

(4) Under Canadian GAAP, liabilities assumed on the purchase of a business may include benefits to be paid employees for their voluntary termination provided certain criteria are met. The treatment of these costs as an assumed liability results in an increase in goodwill recognized on the acquisition. Under US GAAP, a liability and expense for such benefits is required to be expensed by the acquirer in the period employees accept the offer rather than as an adjustment of goodwill.

(5) Under Canadian GAAP, aircraft introduction costs are deferred and amortized. Effective in 1999 under US GAAP, these costs are expensed as incurred.

(6) Under Canadian GAAP, the Corporation has adopted retroactively with restatement, the accounting for the sale of mileage credits to third parties under its loyalty programs (note 18). Under US GAAP, changes in accounting policies are recognized in income in the year of the change.

(7) The income tax recovery (provision) adjustment includes the income tax effect of the above US GAAP/Canadian GAAP adjustments. It also reflects that under Canadian GAAP, the liability method of accounting for income taxes requires that accumulated tax balances be adjusted to reflect substantively enacted changes in future tax rates and regulations. Under US GAAP, tax balances are calculated using currently enacted tax rates and regulations.

(8) Under Canadian GAAP, investments accounted for by the cost method are not restated retroactively to the equity method when the investor acquires control of the business and thus consolidates the investment. US GAAP requires this restatement. As a result of the retroactive application of the equity method under US GAAP, goodwill and related amortization expense reported for the acquisition under Canadian GAAP differs from that reported for US GAAP.

(9) Included in net income is a gain on the purchase of Japanese yen subordinated perpetual debt of $46, $31 after tax (1999 $56, $38 after tax) that for US GAAP reporting purposes is classified as an extraordinary gain. Under US GAAP the calculation of earnings per share is disclosed before extraordinary gains (13).

(10) During 2000, under Canadian GAAP, CICA #3461 (note 18) was applied in a manner that produced recognized and unrecognized amounts for employee future benefit plans the same as those determined by the application of US GAAP with the exception of the recognition of a minimum pension liability adjustment.

(11) Under Canadian GAAP, portfolio investments are accounted for using the cost method. Under US GAAP, portfolio investments classified as available-for-sale securities are carried at market values with unrealized gains or losses included in comprehensive income and as a separate component of shareholders' equity.

(12) Under US GAAP, comprehensive income must be reported which is defined as all changes in equity other than those resulting from investments by owners and distributions to owners. Cumulative comprehensive income as at December 31, 2000 was $4 (1999 $45).

(13) Under US GAAP, the calculation of income per share is based on basic common share equivalents of 120,064,026 (1999 183,320,806) and dilutive potential common shares of 123,353,875 (1999 184,303,639).

	2000	1999
Earnings (loss) per common share before revenue recognition adjustment (6) and extraordinary item (9)	$ (1.03)	$ 1.80
Earnings (loss) per common share before extraordinary item (9)	$ (2.23)	$ 1.80
Earnings (loss) per common share after extraordinary item (9)	$ (1.98)	$ 2.01
Earnings (loss) per common share assuming dilution before revenue recognition adjustment (6) and extraordinary item (9)	$ (1.03)	$ 1.79
Earnings (loss) per common share assuming dilution before extraordinary item (9)	$ (2.23)	$ 1.79
Earnings (loss) per common share assuming dilution after extraordinary item (9)	$ (1.98)	$ 2.00

(14) Recent U.S. accounting pronouncements include Financial Accounting Standards Board Statement 133, Accounting for Derivative Instruments and Hedging Activities ("FAS 133"). Beginning January 1, 2001, FAS 133 requires certain derivatives be recorded in its statement of financial position at fair value. Derivatives that are not designated as hedges must be adjusted to fair value through income. Information on certain financial instruments is described in notes 7, 13 and 15 to the consolidated financial statements. The Corporation has decided not to adopt hedge accounting, is continuing to complete the identification of derivatives and has not yet determined the effect of adoption of FAS 133 upon its consolidated financial statements under US GAAP.

Ten Year Comparative Review [1][2]

Financial data – consolidated ($ millions)

	2000	1999	1998	1997	1996	1995	1994	1993	1992	1991
Operating revenues:										
Passenger	**7,949**	5,520	4,977	4,533	3,980	3,581	3,172	2,849	2,813	2,815
Cargo	**542**	387	369	387	347	323	334	335	342	354
Other	**792**	536	552	612	513	573	495	414	346	316
	9,283	6,443	5,898	5,532	4,840	4,477	4,001	3,598	3,501	3,485
Operating expenses:										
Salaries, wages and benefits	**2,570**	1,760	1,594	1,428	1,323	1,235	1,187	1,136	1,204	1,199
Aircraft fuel [3]	**1,371**	622	657	712	640	527	474	397	472	515
Depreciation, amortization and obsolescence	**405**	311	292	258	258	216	206	219	206	190
Aircraft rent	**705**	513	474	383	319	292	230	214	164	156
Airport and navigation fees	**657**	492	375	228	200	183	161	139	142	128
Other	**3,311**	2,368	2,411	2,230	1,914	1,758	1,538	1,430	1,474	1,461
	9,019	6,066	5,803	5,239	4,654	4,211	3,796	3,535	3,662	3,649
Operating income (loss) before the undernoted item	**264**	377	95	293	186	266	205	63	(161)	(164)
Non-recurring labour expenses	**178**	–	–	–	–	–	–	76	52	36
Operating income (loss)	**86**	377	95	293	186	266	205	(13)	(213)	(200)
Non-operating income (expense):										
Net interest expense	**(210)**	(154)	(174)	(134)	(157)	(201)	(185)	(191)	(190)	(126)
Amortization of deferred foreign exchange	**(24)**	(18)	(32)	(20)	(46)	(69)	(67)	(34)	(17)	(5)
Gain (loss) on sale of investments and other assets	**15**	57	30	236	133	74	133	33	(29)	(5)
Provision for investments and writedown of goodwill	**–**	–	–	–	–	–	–	(111)	(15)	(17)
Other	**6**	(1)	3	16	8	3	32	(14)	–	(8)
Total non-operating income (expense)	**(213)**	(116)	(173)	98	(62)	(193)	(87)	(317)	(251)	(161)
Income (loss) before income taxes and minority interest	**(127)**	261	(78)	391	124	73	118	(330)	(464)	(361)
Recovery of (provision for) income tax	**45**	(121)	34	(39)	(4)	(20)	(25)	(9)	(4)	142
Minority interest	**–**	–	–	–	–	–	(3)	(1)	(2)	1
Income (loss) for the year	**(82)**	140	(44)	352	120	53	90	(340)	(470)	(218)
Effect of accounting policy changes on operating income (loss) [1]	**–**	(126)	(49)	(75)	(29)	(9)	(39)	(14)	(16)	–
Effect of accounting policy changes on income (loss) for the year [1]	**–**	(73)	(28)	(75)	(29)	(9)	(39)	(14)	(16)	
Cash flows from (used for):										
Operating	**115**	680	284	366	64	59	44	(34)	(243)	(221)
Financing	**257**	(515)	72	(266)	(218)	380	(359)	335	246	742
Investing	**(456)**	(10)	(640)	95	(166)	(263)	69	126	287	(829)
Increase (decrease) in cash and cash equivalents	**(84)**	155	(284)	195	(320)	176	(246)	427	290	(308)
Cash and cash equivalents, end of year	**437**	521	366	650	455	775	599	845	418	128
Operating margin before non-recurring labour expenses	**2.8%**	5.9%	1.6%	5.3%	3.8%	5.9%	5.1%	1.8%	(4.6)%	(4.7)%
EBITDAR before non-recurring labour expenses [4]	**1,374**	1,201	861	934	763	774	641	496	209	182
EBITDAR margin before non-recurring labour expenses	**14.8%**	18.6%	14.6%	16.9%	15.8%	17.3%	16.0%	13.8%	6.0%	5.2%
Current ratio	**0.62**	0.84	0.81	1.17	0.92	0.90	1.32	1.36	1.09	1.15
Total assets	**9,721**	6,796	6,503	6,083	5,540	5,436	4,986	5,030	4,782	4,921
Long-term debt (including current portion)	**3,300**	2,414	2,065	1,879	2,142	2,421	2,464	2,640	2,492	2,183
Subordinated perpetual debt	**840**	882	931	931	931	931	931	931	883	834
Shareholders' equity	**316**	363	1,168	1,174	799	676	217	121	221	691
Debt (excluding perpetual debt) to debt plus equity [5]	**73%**	60%	45%	37%	49%	51%	62%	63%	65%	57%
Earnings (loss) per share [6]	**$ (0.69)**	$ 0.75	$ (0.26)	$ 1.98	$ 0.67	$ 0.30	$ 0.70	$ (4.40)	$ (6.34)	$ (2.94)
Cash flow per share from operations [6]	**$ 0.87**	$ 3.61	$ 1.53	$ 2.04	$ 0.41	$ 0.41	$ 0.37	$ (0.44)	$ (3.28)	$ (2.99)
Book value per share	**$ 2.63**	$ 3.03	$ 6.21	$ 7.49	$ 5.13	$ 4.36	$ 1.83	$ 1.03	$ 2.99	$ 9.33
Average common shares outstanding (millions)	**150.7**	189.6	190.3	189.1	189.1	168.7	143.5	80.7	75.9	75.1
Return on equity	**(24)%**	13%	(4)%	36%	16%	12%	53%	(199)%	(103)%	(27)%

(1) 1994 through 1999 restated for accounting policy changes related to loyalty programs and employee future benefits.
1992 and 1993 restated for accounting policy change related to employee future benefits. Refer to note 18 to the consolidated financial statements.
(2) Includes Canadian Airlines from July to December 2000.
(3) Includes fuel excise tax rebates of $46 million in 1993 and $2 million in 1997;
repayments of fuel excise tax rebates of $43 million in 1997 and $2 million in 1998.
(4) Earnings (operating income) before interest, taxes, depreciation, amortization and aircraft rent.
(5) Debt includes current portion of long-term debt, bank indebtedness and is net of cash and cash equivalents.
(6) Fully diluted.

Ten Year Comparative Review (cont'd) [1][2]

Operating statistics – mainline operations

	2000	1999	1998	1997	1996	1995	1994	1993	1992	1991
Passenger – scheduled and charter:										
Revenue passengers carried (millions)	**20.3**	15.2	14.8	**14.0**	13.0	10.8	9.9	9.5	9.9	9.9
Revenue passenger miles (millions) [3]	**35,658**	24,242	23,211	**22,788**	20,596	16,747	14,995	13,768	14,391	13,658
Available seat miles (millions)	**49,229**	33,970	32,719	32,061	29,431	26,578	23,730	21,157	21,628	19,953
Passenger load factor	**72.4%**	71.4%	70.9%	**71.1%**	**70.0%**	**63.0%**	63.2%	65.1%	66.5%	68.4%
Yield per revenue passenger mile (cents) [3]	**19.5**	19.8	18.8	**17.5**	**16.4**	18.0	17.7	17.1	16.3	17.3
Yield per available seat mile (cents)	**14.1**	14.1	13.3	**12.5**	**11.5**	11.4	11.2	11.1	10.8	11.9
Cargo – scheduled and charter:										
Revenue ton miles (millions)	**1,125**	863	833	**895**	**783**	707	633	586	532	549
Yield per revenue ton mile (cents)	**46.3**	43.2	42.7	**41.1**	**41.6**	43.3	43.5	47.6	53.1	53.1
Other measures:										
Operating expense per available seat mile (cents) [4][5]	**16.3**	15.9	15.8	**14.3**	**13.4**	13.3	13.2	13.8	14.2	15.6
Operating expense (net of cargo and other non-ASM revenue) per available seat mile (cents) [4][5][6]	**13.6**	13.2	13.2	**11.6**	**10.9**	10.6	10.7	11.2	11.7	12.9
Average number of full-time equivalent employees (thousands)	**31.6**	23.0	22.8	**21.2**	**19.9**	19.6	18.4	18.2	19.4	20.6
Available seat miles per employee (thousands)	**1,560**	1,478	1,433	**1,516**	1,481	1,359	1,288	1,166	1,112	969
Revenue per employee ($ thousands)	**261**	249	229	**230**	**207**	192	177	161	148	141
Average aircraft utilization (hours per day) [7]	**11.1**	10.8	10.3	**10.4**	**10.7**	10.6	10.3	9.6	9.6	9.8
Average aircraft flight length (miles)	**1,157**	1,014	955	944	957	958	946	907	925	898
Fuel price per litre (cents)	**38.0**	24.6	26.3	27.5	26.3	23.5	23.8	24.4	24.6	26.6
Fuel litres (millions)	**3,234**	2,276	2,251	2,235	2,080	1,910	1,707	1,529	1,609	1,627
Operating statistics – consolidated										
Revenue passenger miles (millions)	37,536	25,623	24,479	23,896	21,894	17,905	16,143	14,820	15,519	14,642
Available seat miles (millions)	**52,553**	36,438	35,037	34,117	31,988	28,968	25,991	23,341	23,886	22,031
Passenger load factor	**71.4%**	70.3%	69.9%	70.0%	**68.4%**	61.8%	62.1%	63.5%	65.0%	66.5%
Yield per revenue passenger mile (cents)	**21.2**	21.5	20.3	18.9	18.1	20.0	19.6	19.2	18.1	19.2

Quarterly Financial and Operating Data [1][2]

(unaudited)

	2000					1999				
	Year	Q4	Q3	Q2	Q1	Year	Q4	Q3	Q2	Q1
Financial data – consolidated ($ millions)										
Operating revenues	**9,283**	2,570	3,069	2,008	1,636	**6,443**	1,640	1,784	1,637	1,382
Operating income (loss)	**264**	(267)	300	234	(3)	**377**	66	201	144	(34)
Income (loss) for the period	**(82)**	(274)	101	**124**	(33)	**140**	(1)	99	58	(16)
Cash flows from operations	**115**	(277)	18	**383**	**(9)**	**680**	211	212	282	(25)
Operating statistics – mainline operations										
Revenue passenger miles (millions) [3]	**35,658**	9,777	12,856	**7,265**	**5,760**	**24,242**	5,760	7,380	6,032	5,070
Domestic	**11,522**	3,163	4,061	**2,365**	**1,933**	**8,449**	2,037	2,502	2,132	1,778
International	**24,136**	6,614	8,795	**4,900**	**3,827**	**15,793**	3,723	4,878	3,900	3,292
Available seat miles (millions)	**49,229**	14,784	16,577	**9,466**	**8,402**	**33,970**	**8,603**	9,599	8,277	7,491
Domestic	**15,718**	4,606	5,334	**3,011**	**2,767**	**11,725**	2,893	3,293	2,908	2,631
International	**33,511**	10,178	11,243	**6,455**	**5,635**	**22,245**	5,710	6,306	5,369	4,860
Passenger load factor	**72.4%**	66.1%	77.6%	**76.8%**	**68.6%**	71.4%	67.0%	76.9%	72.9%	67.7%
Domestic	**73.3%**	68.7%	76.1%	**78.5%**	**69.9%**	**72.1%**	70.4%	76.0%	73.3%	67.6%
International	**72.0%**	65.0%	78.2%	75.9%	67.9%	**71.0%**	65.2%	77.4%	72.6%	67.7%
Yield per revenue passenger mile (cents) [3]	**19.5**	19.1	18.5	21.0	20.4	**19.8**	20.7	18.5	20.4	20.0

(1) 1994 through 1999 restated for accounting policy changes related to loyalty programs and employee future benefits.
1992 and 1993 restated for accounting policy change related to employee future benefits. Refer to note 18 to the consolidated financial statements
(2) Includes Canadian Airlines from July to December 2000.
(3) Includes frequent flyer redemptions (1996 to 2000). (Revenue passengers carried excludes multiple flight legs per passenger.)
(4) Before non-recurring labour expenses.
(5) Includes a fuel excise tax rebate in 1993 of $45 million and a repayment of fuel excise tax rebate in 1997 of $43 million (not consolidated).
(6) Represents the net cost of the passenger transportation business, after deducting the revenue impact of cargo and other non-ASM businesses.
(7) Excludes maintenance down-time.
(8) Includes fuel handling expense (1997 to 2000).

Board of Directors

1 John F. Fraser, O.C.
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Air Canada
Winnipeg, Manitoba

2 Robert A. Milton
President and
Chief Executive Officer
Air Canada
Westmount, Quebec

3 William James
Chairman of the Board
Inmet Mining Corporation
Toronto, Ontario

4 Eva Lee Kwok
Chair and
Chief Executive Officer
Amara International
Investment Corp.
West Vancouver,
British Columbia

5 Fernand Lalonde, Q.C.
Counsel
Leduc Leblanc
Westmount, Quebec

6 David A. Ganong
President
Ganong Bros. Limited
St. Stephen, New Brunswick

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(Retired)
McNeil Consumer
Healthcare Canada
Waterloo, Ontario

8 J.V. Raymond Cyr, O.C.
Chairman of the Board
Polyvalor Inc. and
Vice-Chairman of the Board,
ART Advanced Research and
Technologies Inc.
Montreal, Quebec

9 *David P. O'Brien*
Chairman, President and
Chief Executive Officer
Canadian Pacific Limited
Calgary, Alberta

10 Hon. Edward C. Lumley, P.C.
Vice-Chairman
BMO Nesbitt Burns
Ottawa, Ontario

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PFI Group
Lake Forest, Illinois

12 Pierre-Marc Johnson
Senior Counsel
Heenan Blaikie
Montreal, Quebec

13 Hon. W. David Angus, Q.C.
Senior Partner
Stikeman Elliott
Montreal, Quebec

14 *Ronald W. Osborne*
President and
Chief Executive Officer
Ontario Power Generation Inc.
Toronto, Ontario

Investor and Shareholder Information

Price Range and Trading Volume of Air Canada Common Shares

2000	High	Low	Volume
1st Quarter	$18.30	$ 7.80	45,981,127
2nd Quarter	$21.50	$13.75	36,004,926
3rd Quarter	$20.50	$14.40	31,067,015
4th Quarter	$17.50	$12.10	28,243,691
			141,296,759

The above table sets forth the price range and trading volume of the common shares of Air Canada on the Toronto Stock Exchange

Price Range and Trading Volume of Air Canada Class "A" Shares

2000	High	Low	Volume
1st Quarter	$16.35	$ 7.00	14,763,953
2nd Quarter	$19.25	$11.90	8,582,354
3rd Quarter	$18.10	$11.75	8,359,069
4th Quarter	$15.45	$10.00	4,376,137
			36,081,513

The above table sets forth the price range and trading volume of the Class A Non-voting shares of Air Canada on the Toronto Stock Exchange

Price Range and Trading Volume of Air Canada Class "A" Shares on The Nasdaq Market

2000	High	Low	Volume
1st Quarter	$11.188	$4.875	1,106,243
2nd Quarter	$12.750	$7.938	388,799
3rd Quarter	$12.125	$8.031	338,943
4th Quarter	$10.000	$6.250	336,386
			2,170,371

The above table sets forth the price* range and trading volume of the Class A Non-voting shares of Air Canada on the NASDAQ National Market.

*Prices are quoted in U.S. dollars)

Duplicate Communication

Shareholders receiving more than one copy are requested to call 1-800-387-0825 or write to the Transfer Agent and Registrar, CIBC Mellon Trust Company at the following address: 2001 University Street, Suite 1600, Montreal, Quebec, H3A 2A6. Inquiries may be submitted by electronic mail to inquiries@cibcmellon.ca

Restraints on Air Canada Shares

The Air Canada Public Participation Act and Air Canada's Articles of Continuance limit ownership of the airline's voting shares by all non-residents of Canada to a maximum of 25 per cent. The Canada Transportation Act, (CTA) requires inter alia that at least 75 per cent of the voting shares of Air Canada be owned or controlled by Canadians, as defined in section 55 of the CTA. In addition, no person or group of associated persons may own more than 10% of the airline's voting shares. At the Annual and Special Meeting of Shareholders, shareholders will be invited to consider and approve the adoption of a special resolution relative to amending the Articles of the Corporation for purposes of increasing the ownership threshold from 10% to 15%.

Shareholder Base

Air Canada's shareholder base is comprised of the following: approximately 80 percent institutional; 14 percent, retail and six percent, employees. Eighty-six percent of the voting shares are held by Canadian residents and 14 percent by non-residents (as defined in the Air Canada Public Participation Act and Air Canada's Articles of Continuance).

For Further Information

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Shareholder Relations Director
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Stock Exchange Listings
Toronto Stock Exchange and
The Nasdaq Stock Market.

Internet:
http://www.aircanada.ca

Air Canada complies with the guidelines adopted by the Toronto Stock Exchange. A report on governance matters is included in the March 14, 2001 Management Proxy Circular.

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GLOSSARY OF TERMS

Revenue Passenger Miles (RPMs)
Total number of revenue passengers carried multiplied by the miles they are carried.

Available Seat Miles (ASMs)
A measure of passenger capacity calculated by multiplying the total number of seats available for revenue traffic by the miles flown.

Passenger Load Factor
A measure of passenger capacity utilization derived by expressing revenue passenger miles as a percentage of available seat miles.

Revenue Ton Miles (RTMs)
Total number of cargo tons carried multiplied by the miles they are carried.

Yield
Average revenue per revenue passenger mile or revenue ton mile.

Ce rapport annuel est publié dans les deux langues officielles du Canada. Pour en recevoir un exemplaire en français, écrire à la Secrétaire adjointe et Directrice – Relations avec les actionnaires.

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AIR CANADA

CORPORATE PROFILE

Air Canada is Canada's largest domestic and international full-service airline, providing scheduled and charter air transportation for passengers and for cargo. Air Canada acquired Canadian Airlines International in 2000, becoming the 7th largest North American airline and 12th largest airline in the world. With the acquisition of Canadian, Air Canada is carrying 30 million passengers annually and at year-end employed approximately 45,000 employees.

Air Canada, together with its regional airline subsidiary, serves 150 direct destinations with its fleet of 375 aircraft. Air Canada's primary hubs are located in Toronto, Montreal and Vancouver, each of which has extensive access to domestic, transborder and international markets. Through commercial agreements with other affiliated regional airlines, an additional 38 North American communities are served for a total of 188 direct destinations on five continents. Air Canada with its affiliates is the largest provider of scheduled passenger services in the Canada-US transborder market, Canada-Europe and Canada-Pacific Rim markets. The airline's cargo division serves numerous destinations in Canada and internationally, with sales representation in some 80 countries.

The airline operates an extended global network in conjunction with its international partners. Air Canada is a founding member of Star Alliance, the world's largest and most comprehensive airline alliance group. Other founding members are United Airlines, Lufthansa, Scandinavian Airlines System (SAS) and Thai. They were joined in 1997 by Brazil's VARIG, in 1999 by Air New Zealand, Ansett Australia and All Nippon Airways of Japan, and in 2000 by Singapore Airlines, Mexicana, British Midland and Austrian Airlines Aviation Group. Through its strategic and commercial partnerships with Star Alliance members and several other airlines, Air Canada offers service to over 800 destinations in more than 130 countries.

Air Canada encourages brand loyalty for its services and generates significant revenues through its frequent flyer program, Aeroplan, which has over six million members, and through credit card and other merchant affiliations. Air Canada holds a 100 per cent interest in Air Canada Vacations (Touram Inc.), a major Canadian tour operator. Air Canada also operates a large aircraft and engine maintenance business providing maintenance services to airlines and other customers, and provides other airlines with ground handling and other contract services.

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