ACE AVIATION

Quarter 1 2008
Management's Discussion and Analysis of Results of Operations and Financial Condition

May 9, 2008

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1. Preface

ACE Aviation Holdings Inc. ("ACE"), which was incorporated on June 29, 2004, is a holding company of various aviation interests. In Quarter 1 2008, ACE had two reportable segments: Air Canada and CIE. During 2007, in addition to Air Canada and CIE, ACE had the following additional reportable segments: Aeroplan Limited Partnership ("Aeroplan") up to March 14, 2007, Jazz Air LP ("Jazz") up to May 24, 2007 and ACTS LP ("ACTS") up to October 16, 2007.

ACE is listed on the Toronto Stock Exchange ("TSX") where its Class A variable voting shares and Class B voting shares are traded under the symbols ACE.A and ACE.B, respectively.

This Management's Discussion and Analysis of Results of Operations and Financial Condition ("MD&A") for Quarter 1 2008 should be read in conjunction with ACE's unaudited interim consolidated financial statements and notes for Quarter 1 2008. Reference to "Corporation" in this MD&A refers to, as the context may require, ACE and its aviation interests collectively, ACE and one or more of its aviation interests, one or more of ACE's aviation interests, or ACE itself. Except where the context otherwise requires, all monetary amounts are stated in Canadian dollars. For an explanation of certain terms used in this MD&A, refer to section 16 "Glossary of Terms". Except as otherwise noted, this MD&A is current as of May 8, 2008.

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

The ACE Audit, Finance & Risk Committee has reviewed this MD&A and the Quarter 1 2008 unaudited interim consolidated financial statements and notes and ACE's Board of Directors approved these documents prior to their release. For further information on ACE's public disclosure file, including ACE's Annual Information Form, please consult SEDAR at www.sedar.com, EDGAR at www.sec.gov/edgar.shtml or ACE's website at www.aceaviation.com.

2. Caution Regarding Forward-Looking Information

ACE's communications often contain written or oral forward-looking statements which are included in the MD&A and may be included in filings with securities regulators in Canada and the United States. These forward-looking statements are identified by the use of terms and phrases such as "anticipate", "believe", "could", "estimate", "expect", "intend", "may", "plan", "predict", "project", "will", "would", and similar terms and phrases, including references to assumptions. Such statements may involve but are not limited to comments with respect to strategies, expectations, planned operations or future actions.

Forward-looking statements, by their nature, are based on assumptions and are subject to important risks and uncertainties. Any forecasts or forward-looking predictions or statements cannot be relied upon due to, amongst other things, changing external events and general uncertainties of the business. Results indicated in forward-looking statements may differ materially from actual results for a number of factors, including without limitation, energy prices, general industry, market and economic conditions, war, terrorist acts, changes in demand due to the seasonal nature of the business, the ability to reduce operating costs and employee counts, employee relations, labour negotiations or disputes, pension issues, currency exchange and interest rates, changes in laws, adverse regulatory developments or proceedings, pending litigation and actions by third parties as well as the factors identified throughout this MD&A and, in particular, those identified in the "Risk Factors" section of ACE's 2007 MD&A dated February 7, 2008 and section 10 of this MD&A. The forward-looking statements contained in this discussion represent ACE's expectations as of May 8, 2008, and are subject to change after such date. However, ACE disclaims any intention or obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise, except as required under applicable securities regulations.

3. Industry Interests

The following is a listing of ACE's aviation interests as at May 8, 2008.

	Aviation Interests	Ownership
Air Canada (TSX: AC.A, AC.B)	Air Canada is Canada's largest domestic and international airline and the largest provider of scheduled passenger services in the Canadian market, the Canada - US transborder market and in the international market to and from Canada. Wholly-owned subsidiaries of Air Canada include: • AC Cargo Limited Partnership ("Air Canada Cargo") which, together with Air Canada, are Canada's largest provider of air cargo services. • ACGHS Limited Partnership ("Air Canada Ground Handling Services") which is a passenger and ground handling service provider. • Touram Limited Partnership ("Air Canada Vacations") which is a major Canadian tour operator offering leisure travel packages.	75.0 %
Aeroplan (TSX: AER.UN)	Aeroplan is Canada's premier loyalty marketing program. Aeroplan provides its commercial partners with loyalty marketing services designed to stimulate demand for such partners' products and services. ACE's ownership interest in Aeroplan is held indirectly through its holdings of Aeroplan Income Fund units. On December 20, 2007, Aeroplan acquired privately-held LMG, a leading loyalty marketing and customer-driven insight and analysis company.	9.9%
Jazz (TSX: JAZ.UN)	Jazz is the largest regional airline and second largest airline in Canada, after Air Canada, based on fleet size and number of routes operated. Jazz operates both domestic and US transborder services for Air Canada under a capacity purchase agreement. ACE's ownership interest in Jazz is indirectly held through its holdings of Jazz Air Income Fund units.	9.5%
ACTS Aero	ACTS Aero is a full-service aircraft maintenance, repair and overhaul organization that competes on a global basis.	22.8%

4. Significant Events

The following significant events occurred during the period January 1, 2008 to May 8, 2008.

Substantial Issuer Bid

On January 10, 2008, ACE accepted for purchase and cancellation a total of 40,023,427 Class A variable voting shares and 9,894,166 Class B voting shares at $30.00 per share for an aggregate purchase price of $1,498 million, in accordance with the terms of a substantial issuer bid. No convertible preferred shares of ACE were deposited on an as converted basis under the offer.

ACTS

On January 14, 2008, cash proceeds of $40 million, representing the full balance of funds held in escrow on the closing of the monetization of ACTS on October 16, 2007, were received by ACE.

Jazz

On January 24, 2008, ACE sold 13,000,000 units of Jazz Air Income Fund on an exempt trade basis to certain funds and accounts managed by West Face Capital Inc. and to Sunrise Partners Limited Partnership at a price of $7.45 per unit representing total net proceeds to ACE of approximately $97 million.

Aeroplan

On April 21, 2008, ACE completed the sale of 20,400,000 units of Aeroplan Income Fund at a price of $17.50 per unit, for gross proceeds of $357 million (net proceeds of approximately $343 million). Immediately following the sale, ACE held 19,892,088 units of Aeroplan Income Fund, representing approximately 9.9% of the issued and outstanding units of Aeroplan Income Fund.

5. Accounting Policies

ACE prepares its consolidated financial statements in accordance with Canadian Generally Accepted Accounting Principles ("GAAP").

Significant accounting policies and methods used in preparation of ACE's Quarter 1 2008 unaudited interim consolidated financial statements are described in Note 2 to ACE's 2007 audited consolidated financial statements.

ACE's results reflect the consolidation of Aeroplan's operations only up to March 14, 2007, the consolidation of Jazz's operations only up to May 24, 2007 and the consolidation of ACTS' operations only up to October 16, 2007. After those dates, ACE's investments in Aeroplan, ACTS Aero and Jazz (up to February 7, 2008) are accounted for using the equity method. Effective February 7, 2008, ACE's investment in Jazz is classified as an available-for-sale investment. As a result of the above-noted changes, ACE's results of operations for 2008 are not directly comparable to its operating results for 2007.

The preparation of ACE's consolidated financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent liabilities and reported amounts of revenues and expenses for the period of the consolidated financial statements. ACE evaluates these estimates and assumptions on a regular basis, based on historical experience and other relevant factors. Actual amounts could differ materially from those estimates and assumptions. For a description of critical accounting estimates utilized in the preparation of ACE's consolidated financial statements, see "Critical Accounting Estimates" in ACE's 2007 MD&A dated February 7, 2008. There were no significant changes to ACE's critical accounting estimates from those disclosed at that time.

Accounting for Aeroplan
As a result of ACE's special distribution of Aeroplan Income Fund units and the conversion of its remaining units of Aeroplan LP into units of Aeroplan Income Fund on March 14, 2007, ACE no longer consolidates the results of operations, assets and liabilities and cash flows of Aeroplan after that date and accounts for its investment using the equity method of accounting.

Accounting for Jazz
As a result of the special distribution of Jazz Air Income Fund units on May 24, 2007, ACE no longer consolidated the results of operations, assets and liabilities and cash flows of Jazz after that date and accounted for its investment from May 24, 2007 to February 7, 2008 using the equity method of accounting. Subsequent to ACE's sale of Jazz Air Income Fund units on January 24, 2008 and the termination of the Securityholders' Agreement between ACE and Jazz Air Income Fund on February 7, 2008, ACE no longer equity accounts for Jazz and ACE's investment in Jazz is classified as an available-for-sale investment under financial instruments. Unrealized period changes in fair value are recorded in "other comprehensive income" and distributions from Jazz Air Income Fund are recorded in "equity and other investment income" in non-operating expense income (expense) on ACE's consolidated statement of operations.

Accounting for ACTS
As a result of the monetization of ACTS on October 16, 2007, ACE no longer consolidates the results of operations, assets and liabilities and cash flows of ACTS after that date and accounts for its investment using the equity method of accounting.

Changes in Accounting Policies

Capital Disclosures and Financial Instruments – Presentation and Disclosure

Effective January 1, 2008, the Corporation adopted three new CICA accounting standards: section 1535, *Capital Disclosures*, section 3862, *Financial Instruments – Disclosures* and section 3863, *Financial Instruments – Presentation*.

Section 1535 establishes disclosure requirements about an entity's capital and how it is managed. The purpose is to enable users of the financial statements to evaluate the entity's objectives, policies and processes for managing capital.

Sections 3862 and 3863 replace section 3861, *Financial Instruments – Disclosure and Presentation*, revising and enhancing its disclosure requirements in certain areas, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. Refer to section 9 of this MD&A for information on the Corporation's financial instruments.

For additional information on these new accounting standards, refer to sections 7.6 and 9 of this MD&A.

Inventories

Effective January 1, 2008, the Corporation adopted CICA section 3031, *Inventories*, which replaced section 3030, *Inventories*. Section 3031 provides more extensive guidance on measurement, and expands disclosure requirements to increase transparency. The Corporation's accounting policy for aircraft fuel inventory is consistent with the measurement requirements in the new standard and, as a result, no adjustment was recorded on the transition, however, additional disclosures have been included in ACE's interim unaudited consolidated financial statements for Quarter 1 2008.

Future Accounting Standard Changes

In February 2008, the CICA issued section 3064, *Goodwill and Intangible Assets,* which provides guidance on the recognition, measurement, presentation and disclosure for goodwill and intangible assets, other than the initial recognition of goodwill or intangible assets acquired in a business combination. The standard is effective for fiscal years beginning on or after October 1, 2008, and requires retroactive application to prior period financial statements. The Corporation is in the process of evaluating the impact of this new standard for adoption on January 1, 2009.

6. Results of Operations – Quarter 1 2008

The following table reflects the results of the Corporation, the results of its reportable segments and certain non-GAAP measures for Quarter 1 2008. Segment information has been prepared consistent with how financial information is produced internally for the purposes of making business decisions.

Unaudited (Canadian dollars in millions)	Quarter 1 2008		
	Air Canada	CIE	ACE Total
Operating revenue			
Passenger revenue	$ 2,311	$ -	$ 2,311
Cargo revenue	124	-	124
Other revenue	291	-	291
External revenue	2,726	-	2,726
Inter-segment revenue	1	(1)	-
	2,727	(1)	2,726
Operating expenses			
Wages, salaries and benefits	481	15	496
Aircraft fuel	715	-	715
Aircraft rent	63	-	63
Airport and navigation fees	241	-	241
Aircraft maintenance, materials, and supplies	203	-	203
Communications and information technology	73	-	73
Food, beverages and supplies	77	-	77
Depreciation, amortization and obsolescence	171	(2)	169
Commissions	53	-	53
Capacity purchase with Jazz	235	-	235
Other operating expenses	427	1	428
	2,739	14	2,753
Operating loss before under-noted item	**(12)**	**(15)**	**(27)**
Provision for cargo investigations	(125)	-	(125)
Operating loss	**(137)**	**(15)**	**(152)**
Non-operating income (expense)			
Interest income	18	7	25
Interest expense	(81)	(15)	(96)
Interest capitalized	17	-	17
Gain (loss) on disposal of assets	(36)	82	46
Loss on financial instruments recorded at fair value	(23)	-	(23)
Equity and other investment income [(1)]	-	12	12
Other non-operating income (expense)	(2)	1	(1)
	(107)	87	(20)
Income (loss) before the following items	**(244)**	**72**	**(172)**
Non-controlling interest	(3)	67	64
Foreign exchange loss	(89)	-	(89)
Recovery of (provision for) income taxes	48	(33)	15
Income (loss) for the period	**(288)**	**106**	**(182)**
EBITDAR/EBITDA before the provision for cargo investigations [(2)]	**$ 222**	**$ (17)**	**$ 205**
EBITDAR/EBITDA [(2)]	**$ 97**	**$ (17)**	**$ 80**

(1) ACE is accounting for its investments in Aeroplan, ACTS Aero and Jazz (up to February 7, 2008) under the equity method and, for Quarter 1 2008, has recorded equity income from these investments in non-operating income (expense) under "equity and other investment income" within the CIE segment. Effective February 7, 2008, distributions from Jazz Air Income Fund are recorded in "equity and other investment income" within CIE.

(2) Refer to section 15 "Non-GAAP Financial Measures" in this MD&A for a reconciliation of EBITDAR before the provision for cargo investigations to operating income (loss) and EBITDAR/EBITDA to operating income (loss).

The following table reflects the results of the Corporation, the results of its reportable segments and certain non-GAAP measures for Quarter 1 2007.

Unaudited	Quarter 1 2007					
(Canadian dollars in millions)	Air Canada	Aeroplan [1]	Jazz	ACTS	CIE	ACE Total
Operating revenue						
Passenger revenue	$ 2,137	$ -	$ -	$ -	$ 15	$ 2,152
Cargo revenue	140	-	-	-	-	140
Other revenue	209	198	2	57	(133)	333
External revenue	2,486	198	2	57	(118)	2,625
Inter-segment revenue	54	3	362	196	(615)	-
	2,540	**201**	**364**	**253**	**(733)**	**2,625**
Operating expenses						
Wages, salaries and benefits	499	17	83	86	13	698
Aircraft fuel	585	-	71	-	(71)	585
Aircraft rent	79	-	35	-	(10)	104
Airport and navigation fees	243	-	47	-	(47)	243
Aircraft maintenance, materials, and supplies	224	-	30	79	(197)	136
Communications and information technology	71	7	1	4	(7)	76
Food, beverages and supplies	80	-	4	-	(1)	83
Depreciation, amortization and obsolescence	128	3	5	9	1	146
Commissions	59	-	-	-	-	59
Capacity purchase with Jazz	230	-	-	-	(230)	-
Special charge for labour restructuring	-	-	-	9	-	9
Other operating expenses	420	134	52	63	(154)	515
	2,618	161	328	250	(703)	2,654
Operating income (loss)	**(78)**	**40**	**36**	**3**	**(30)**	**(29)**
Non-operating income (expense)						
Interest income	26	3	1	-	3	33
Interest expense	(91)	(3)	(2)	(5)	(22)	(123)
Interest capitalized	36	-	-	-	-	36
Gain on disposal of assets	7	-	-	-	-	7
Gain on financial instruments recorded at fair value	34	-	-	-	-	34
Equity and other investment income	-	-	-	-	3	3
Other non-operating income (expense)	(4)	(1)	-	-	5	-
	8	(1)	(1)	(5)	(11)	(10)
Income (loss) before the following items	**(70)**	**39**	**35**	**(2)**	**(41)**	**(39)**
Non-controlling interest	(2)	-	-	-	(21)	(23)
Foreign exchange gain	33	-	-	-	-	33
Recovery of (provision for) income taxes	5	-	-	-	(48)	(43)
Income (loss) for the period	**$ (34)**	**$ 39**	**$ 35**	**$ (2)**	**$ (110)**	**$ (72)**
EBITDAR/EBITDA [2]	**$ 129**	**$ 43**	**$ 76**	**$ 12**	**$ (39)**	**$ 221**

(1) *The above reflects the consolidation of Aeroplan results from January 1 to March 13, 2007. Commencing March 14, 2007, ACE is accounting for its investment in Aeroplan under the equity method and, for the period March 14 to March 31, 2007, has recorded equity income from the Aeroplan investment in non-operating income (expense) under "equity and other investment income" within the CIE segment.*

(2) *Refer to section 15 "Non-GAAP Financial Measures" in this MD&A for a reconciliation of EBITDAR/EBITDA to operating income (loss).*

ACE's results of operations and EBITDAR for Quarter 1 2008 are not directly comparable to its operating results and EBITDAR for Quarter 1 2007. Refer to section 5 of this MD&A for additional information on the changes in accounting relating to Aeroplan, Jazz and ACTS Aero.

ACE recorded an operating loss of $27 million, before a provision for cargo investigations, in Quarter 1 2008 compared to an operating loss of $29 million in Quarter 1 2007. Air Canada recorded a provision for cargo investigations of $125 million in Quarter 1 2008 relating to alleged anti-competitive cargo pricing activities. Management does not consider this provision to be reflective of the underlying financial performance of Air Canada from ongoing operations. ACE's consolidated results for Quarter 1 2007 included operating income from Aeroplan, Jazz and ACTS of $40 million, $36 million and $3 million, respectively.

EBITDAR of $205 million, before the provision for cargo investigations, was recorded in Quarter 1 2008 compared to EBITDAR of $221 million in the same period in 2007. In Quarter 1 2007, Aeroplan, Jazz and ACTS recorded EBITDAR of $43 million, $76 million and $12 million, respectively.

ACE recorded operating revenues of $2,726 million and operating expenses of $2,753 million in Quarter 1 2008. In the same period in 2007, ACE recorded operating revenues of $2,625 million and operating expenses of $2,654 million. As a result of the deconsolidation of Aeroplan, Jazz and ACTS, ACE's Quarter 1 2008 operating revenues and expenses are not directly comparable to its operating revenues and expenses for Quarter 1 2007.

Non-operating expense amounted to $20 million in Quarter 1 2008 compared to non-operating expense of $10 million in Quarter 1 2007. Included in Quarter 1 2008 was a gain on ACE's sale of Jazz Air Income Fund units of $89 million and an impairment charge of $38 million recorded by Air Canada related to its fleet of Boeing 767-200 aircraft due to the revised retirement date of the aircraft. Losses on financial instruments recorded at fair value amounted to $23 million in Quarter 1 2008 compared to gains of $34 million in Quarter 1 2007. Refer to section 9 of this MD&A for additional information on Air Canada's derivatives.

Net losses on foreign currency monetary items amounted to $89 million in Quarter 1 2008 versus gains of $33 million in Quarter 1 2007. The loss in Quarter 1 2008 was largely attributable to a weaker Canadian dollar at March 31, 2008 compared to December 31, 2007, partially offset by gains of $79 million related to foreign currency derivatives. The March 31, 2008 noon date rate was $1US = Cdn $1.0279 while the December 31, 2007 noon date rate was $1US = Cdn $0.9881.

Income tax recovery was $15 million in Quarter 1 2008 on a pre-tax loss of $197 million. No tax recovery was recorded by Air Canada on the provision for cargo investigations. A provision for income taxes of $43 million was recorded in Quarter 1 2007 on a pre-tax loss of $29 million, mainly related to non-recurring items including the special distribution of Aeroplan Income Fund and Jazz Air Income Fund units.

Net loss in Quarter 1 2008 amounted to $182 million or $(2.96) per diluted share. Net loss in Quarter 1 2007 amounted to $72 million or $(0.70) per diluted share. The net loss in Quarter 1 2008 included the provision of $125 million recorded by Air Canada related to alleged anti-competitive cargo pricing activities.

6.1. Air Canada

In Quarter 1 2008, Air Canada recorded an operating loss of $12 million, before the provision for cargo investigations, compared to an operating loss of $78 million in Quarter 1 2007, an improvement of $66 million.

In Quarter 1 2008, EBITDAR amounted to $222 million, before the provision for cargo investigations, compared to EBITDAR of $129 million in the same period in 2007, an improvement of $93 million, despite an increase in fuel expense of $130 million.

Passenger revenues increased $174 million or 8.1% to $2,311 million in Quarter 1 2008 due to traffic growth of 4.4% and a yield increase of 2.2%, despite the negative impact of a stronger Canadian dollar discussed further below. System RASM increased 2.0% due to the growth in yield. The North American market remained strong with domestic passenger revenues increasing by $74 million or 8.7% from Quarter 1 2007, due to both yield and traffic growth, and US transborder passenger revenues increasing by $41 million or 8.4% from Quarter 1 2007, due to an increase in yield. In the Atlantic market, passenger revenues increased $12 million or 3.4% from Quarter 2007, due primarily to traffic and, to a lesser extent, yield growth. Pacific passenger revenues decreased $7 million or 3.1% from Quarter 1 2007, due to a decline in yield. Other passenger revenues (comprised of South Pacific, Caribbean, Mexico and South America) increased $54 million or 23.1% from Quarter 1 2007. A stronger Canadian dollar in Quarter 1 2008, which lowers the Canadian dollar value of sales in foreign countries, had a negative impact on foreign currency denominated revenues, accounting for a decrease of $62 million to Air Canada's Quarter 1 2008 passenger revenues.

Operating expenses were $2,739 million in Quarter 1 2008, an increase of $121 million or 5% over Quarter 1 2007, largely due to higher fuel expense which increased $130 million or 22% from Quarter 1 2007. CASM in Quarter 1 2008 was unchanged from Quarter 1 2007. Excluding fuel expense, CASM declined 4.8%. Unit cost reductions were recorded in all major categories with the exception of fuel and ownership costs. A stronger Canadian dollar versus the US dollar and unit cost savings related to the Boeing 777 aircraft were among the more important factors in the unit cost decrease, excluding fuel expense, from the first quarter of 2007. The higher unit cost of ownership reflects Air Canada's investment in new aircraft and the aircraft interior refurbishment program.

Non-operating expense amounted to $107 million in Quarter 1 2008 compared to non-operating income of $8 million in Quarter 1 2007. Net interest expense increased $17 million. A lower amount of capitalized interest related to new aircraft and a decrease in interest income due to lower cash balances more than offset a $10 million decrease in interest expense. Although there was an increase in interest expense driven by the financing of additional aircraft in the quarter, this increase was more than offset by the impact of lower aircraft financing rates versus Quarter 1 2007 and the favourable impact of a stronger Canadian dollar versus the US dollar in Quarter 1 2008 compared to Quarter 1 2007.

In Quarter 1 2008, Air Canada recorded an impairment charge of $38 million related to its fleet of Boeing 767-200 aircraft due to the revised retirement date of the aircraft. Losses relating to fair value adjustment on certain derivatives instruments amounted to $23 million in Quarter 1 2008 versus gains of $34 million in the same quarter of 2007. Losses recorded in Quarter 1 2008 related to derivatives are described in section 9 of this MD&A.

Net losses on foreign currency monetary items amounted to $89 million in Quarter 1 2008 versus gains of $33 million in Quarter 1 2007. The loss in Quarter 1 2008 was largely attributable to a weaker Canadian dollar at March 31, 2008 compared to December 31, 2007, partially offset by gains of $79 million related to foreign currency derivatives.

Income tax recovery was $48 million in Quarter 1 2008, representing an effective income tax rate of 14%, as compared to $5 million at an effective income tax rate of 13% for the same period in 2007. The effective income tax rate was impacted by the capital portion of certain foreign exchange losses reported in Quarter 1 2008 which were tax-effected at 50% of the income tax rate. In addition, no tax recovery was recorded on the provision for cargo investigations, which has the effect of reducing the effective tax rate.

A segment loss of $288 million was recorded in Quarter 1 2008 compared to a segment loss of $34 million in Quarter 1 2007. The segment loss in Quarter 1 2008 included a provision of $125 million related to alleged anti-competitive cargo pricing activities.

6.2. Corporate Items and Eliminations ("CIE")

CIE includes the corporate, financing and investing activities of ACE. As a result of the change in the accounting for ACE's investment in Aeroplan, effective March 14, 2007, certain consolidation adjustments relating to Aeroplan are no longer recorded in CIE. As previously discussed, the accounting for ACE's investment in ACTS Aero was changed during October 2007 from consolidation to the equity method of accounting reported under the CIE segment. Up until the time of deconsolidating ACTS Aero, the CIE segment also included certain consolidation adjustments related to revenue recognition differences for maintenance services provided by ACTS (completed contract basis of accounting for engine and component maintenance services versus the expense recognition basis in Air Canada and Jazz, which is as the work is completed). In addition, consolidation adjustments were previously made related to the timing of revenue and expense recognition pertaining to power-by-the-hour contracts. Subsequent to the change in the accounting for ACE's investment in ACTS, these consolidation adjustments are no longer required.

ACE's consolidated statement of operations for Quarter 1 2008 reflected $12 million of equity and other investment income from ACE's investment in Aeroplan, Jazz and ACTS Aero. Effective February 7, 2008, ACE no longer equity accounts for Jazz. ACE's investment in Jazz is now classified as an available-for-sale investment under financial instruments, resulting in unrealized period changes in fair value being recorded in "other comprehensive income" and distributions from Jazz Air Income Fund being recorded in "equity and other investment income" in the CIE segment. In Quarter 1 2007, equity income of $3 million was recorded by ACE. CIE recorded an operating loss of $15 million in Quarter 1 2008 compared to an operating loss of $30 million in Quarter 1 2007. Negative EBITDAR of $17 million was recorded in Quarter 1 2008 compared to negative EBITDAR of $39 million in Quarter 1 2007.

The sale by ACE of 13,000,000 units of Jazz Air Income Fund resulted in a gain on sale of $89 million ($71 million after tax) in Quarter 1 2008.

7. Financial and Capital Management

The following table summarizes ACE's consolidated statement of financial position as at March 31, 2008 and as at December 31, 2007.

Condensed Consolidated Statement of Financial Position (Canadian dollars in millions)	**March 31, 2008**	**December 31, 2007**
Assets		
Cash, cash equivalents and short-term investments	$ 1,933	$ 3,139
Other current assets	1,420	1,482
Current assets	3,353	4,621
Property and equipment	7,743	7,925
Intangible assets	650	647
Other assets	675	578
	$ 12,421	**$ 13,771**
Liabilities		
Current liabilities	$ 3,372	$ 3,252
Long-term debt and capital lease obligations	4,035	4,006
Pension and other benefits liabilities	1,773	1,824
Other long-term liabilities	862	715
	10,042	**9,797**
Non-controlling interest	**692**	**757**
Shareholders' equity	**1,687**	**3,217**
	$ 12,421	**$ 13,771**

7.1. Analysis of Financial Position

At March 31, 2008, ACE consolidated cash, cash equivalents and short-term investments amounted to $1,933 million, a decrease of $1,206 million from December 31, 2007. ACE's unconsolidated cash, cash equivalents and short-term investments amounted to $539 million, a decrease of $1,361 million from December 31, 2007. The change in ACE's unconsolidated cash balances was mainly the result of the substantial issuer bid, partially offset by the sale and disposals discussed under section 7.2 of this MD&A. Air Canada's cash, cash equivalents and short-term investments amounted to $1,394 million at March 31, 2008, an increase of $155 million from December 31, 2007. Shareholders' equity totaled $1,687 million at March 31, 2008, a reduction of $1,530 million from December 31, 2007. The change in shareholders' equity was mainly due to the substantial issuer bid.

Convertible Senior Notes

In 2005, ACE issued $330 million of Convertible Senior Notes due 2035 which bear interest at a rate of 4.25% per annum ("Convertible Senior Notes"). As at March 31, 2008, Convertible Senior Notes with a face value of $7 million had been converted at the option of the holder and settled for cash resulting in ACE having a principal amount of $323 million in Convertible Senior Notes issued and outstanding.

At any time on or after June 6, 2008, ACE may redeem all or a portion of the Convertible Senior Notes at a redemption price equal to 100% of the principal amount of the Convertible Senior Notes, plus accrued interest. For accounting purposes, the Convertible Senior Notes are presented as a compound instrument. The carrying value of the financial liability component of the Convertible Senior Notes at March 31, 2008 was $277 million.

7.2. Consolidated Cash flows

As previously discussed, ACE's results reflect the consolidation of Aeroplan's operations only up to March 14, 2007, the consolidation of Jazz's operations only up to May 24, 2007 and the consolidation of ACTS' operations only up to October 16, 2007. Consequently, ACE's consolidated statement of cash flows for Quarter 1 2008 is not comparable to its consolidated statement of cash flows for Quarter 1 2007.

The following table summarizes ACE's consolidated statement of cash flows for the indicated periods.

(Canadian dollars in millions)	Quarter 1 2008	Quarter 1 2007	$ Change
Cash from operating activities	$ 229	$ 319	$ (90)
Cash used for financing activities	(1,633)	(1)	(1,632)
Cash from (used for) investing activities	358	(819)	1,177
Net change in cash and cash equivalents during the period	**(1,046)**	**(501)**	**(545)**
Cash and cash equivalents - Beginning of period	**2,300**	**1,854**	**446**
Cash and cash equivalents - End of period	**$ 1,254**	**$ 1,353**	**$ (99)**

ACE unconsolidated

The following summarizes significant transactions or factors which impacted ACE's unconsolidated cash, cash equivalents and short-term investments in Quarter 1 2008:

- A decrease in ACE's cash flows from operations from Quarter 1 2007 was primarily as result of the change in accounting for ACE's investment in Aeroplan and Jazz. Refer to section 5 of this MD&A for information on ACE's accounting policies.

- On January 10, 2008, ACE accepted for purchase and cancellation a total of 40,023,427 Class A variable voting shares and 9,894,166 Class B voting shares at $30.00 per share for an aggregate purchase price of $1,498 million, in accordance with the terms of a substantial issuer bid. This transaction is reflected in "cash used for investing activities" in ACE's Quarter 1 2008 consolidated statement of cash flows.

- On January 14, 2008, cash proceeds of $40 million representing the full balance of funds held in escrow on closing of the monetization of ACTS on October 16, 2007 were received by ACE. This transaction is reflected in "cash from investing activities" in ACE's Quarter 1 2008 consolidated statement of cash flows.

- On January 24, 2008, ACE completed the sale of 13,000,000 units of Jazz Air Income Fund at a price of $7.45 per unit for net proceeds of approximately $97 million. This transaction is reflected in "cash from investing activities" in ACE's Quarter 1 2008 consolidated statement of cash flows.

On April 21, 2008, ACE completed the sale of 20,400,000 units of Aeroplan Income Fund at a price of $17.50 per unit for net proceeds of approximately $343 million. ACE's unconsolidated cash, cash equivalents and short-term investments amounted to $886 million following the sale of these units on April 21, 2008.

In Quarter 1 2007, cash flows used for investing activities included cash payments of $53 million in connection with the acquisition of Aeroman and the Aeroplan cash of $231 million which was removed from ACE's consolidated statement of financial position.

Air Canada
The following summarizes significant transactions or factors which impacted Air Canada's consolidated cash, cash equivalents and short-term investments in Quarter 1 2008:

- Cash flows from operating activities decreased $13 million from Quarter 1 2007. An improvement in operating results compared to Quarter 1 2007 was more than offset by unfavourable changes in non-cash working capital items, mainly attributable to growth in accounts receivable due to the timing of passenger sales.
- Cash used for financing activities in Quarter 1 2008 amounted to $135 million in Quarter 1 2008. Air Canada had new aircraft borrowings of $187 million which were more than offset by reduction of long-term debt and capital lease obligations of $322 million.
- Cash flows from investing activities in Quarter 1 2008 amounted to $159 million. Air Canada received proceeds of $411 million in Quarter 1 2008 relating to the sale and leaseback of three Boeing 777 aircraft. Additions to capital assets at Air Canada, including the expenditures relating to the three Boeing 777 which were sold and leased back, amounted to $403 million. Other additions included one additional Boeing 777 aircraft, three Embraer ERJ-190 aircraft, expenditures related to the aircraft interior refurbishment program and inventory and spare engines. Air Canada sold an Airbus A319 aircraft in Quarter 1 2008 for proceeds of $23 million. In Quarter 1 2007, Air Canada sold one of its commercial real estate properties for net proceeds of $42 million.

7.3. Contractual Obligations

The table below provides the Corporation's current contractual obligations as at March 31, 2008 for the remainder of 2008, for the next four years and after 2012. All obligations are related to Air Canada with the exception of the Convertible Senior Notes which are an ACE unconsolidated obligation. Air Canada's capital expenditure projections, including the pre-delivery payments, have been amended to reflect a delay in the deliveries of the Boeing 787 aircraft. Refer to section 7.5 for additional information on this delay.

Contractual Obligations (Canadian dollars in millions)	Remainder of 2008	2009	2010	2011	2012	Thereafter	Total
Convertible senior notes	$ 330	$ -	$ -	$ -	$ -	$ -	$ 330
Long-term debt obligations [1]	228	293	272	278	281	2,155	3,507
Debt consolidated under AcG-15 [1]	122	105	153	340	93	193	1,006
Capital lease obligations [1]	204	152	147	142	184	588	1,417
Operating lease obligations [2]	220	290	278	214	196	624	1,822
Committed capital expenditures [3]	291	29	53	84	457	3,779	4,693
Foreign exchange derivatives	22	-	-	-	-	-	22
Total contractual obligations [4]	**$ 1,417**	**$ 869**	**$ 903**	**$ 1,058**	**$ 1,211**	**$ 7,339**	**$ 12,797**
Pension funding obligations [5]	$ 266	$ 328	$ 338	$ 348	$ 358	N/A	N/A

(1) *Includes both the principal and the interest component of the payment obligations on long-term debt and capital leases and is based on interest rates and the applicable foreign exchange rate effective as at March 31, 2008.*
(2) *Mainly relate to US dollar aircraft operating leases.*
(3) *Mainly relate to US dollar aircraft-related expenditures. Also include purchases relating to system development costs, facilities and leasehold improvements.*
(4) *Excludes commitments for goods and services required in the ordinary course of business. Also excluded are future income taxes and other long-term liabilities mainly due to reasons of uncertainty of timing of cash flows and items which are non-cash in nature.*
(5) *There were no changes to Air Canada's pension plan funding obligations from those disclosed in ACE's 2007 MD&A dated February 7, 2008.*

7.4. Air Canada Capital Expenditures and Related Financing Arrangements

In 2004, Air Canada signed a definitive purchase agreement with Empresa Brasileira de Aeronautica S.A. ("Embraer") for the acquisition of regional jet aircraft. In November 2005, Air Canada also concluded agreements with The Boeing Company ("Boeing") for the acquisition of Boeing 777 and Boeing 787 aircraft.

Boeing

As at March 31, 2008, 11 of the 16 Boeing 777 firm aircraft under the purchase agreement with Boeing had been delivered, with the remaining five firm deliveries expected to be delivered by November 2008. The seven aircraft delivered in 2007 were financed under a loan guarantee facility with the Export-Import Bank of the United States ("EXIM"). In January 2008, the Corporation received a commitment for loan guarantee support from EXIM for all nine 2008 Boeing 777 firm aircraft deliveries. The loan guarantee, subject to certain conditions, covers a 12-year loan term for 85% of the capital expenditure at an interest rate based on a floating rate. The table below assumes that Air Canada will use the EXIM guarantee facility for five of the nine aircraft in 2008. Air Canada is currently reviewing its financing alternatives and may not utilize EXIM financing on all remaining 2008 deliveries. As at May 8, 2008, five of the nine 2008 Boeing 777 aircraft had been delivered, one of these aircraft was financed using the EXIM facility and the other four aircraft were, concurrently with the purchase, sold and leased back to Air Canada.

As at March 31, 2008, Air Canada had completed the sale and leaseback of three of these Boeing 777 aircraft and the sale and leaseback of a fourth aircraft was completed in April 2008. The four leases are accounted for as operating leases with 12-year terms. All leases are at market rates. These sale and leaseback transactions replace an equivalent number of aircraft loan guarantee commitments provided by EXIM.

Boeing has notified Air Canada that its first Boeing 787 aircraft originally scheduled for delivery in 2010 is now scheduled for delivery in 2012, with additional deliveries, originally scheduled for completion between 2010 and 2014, being delayed by approximately two to two and a half years. Air Canada will be seeking compensation from Boeing and evaluating alternatives to mitigate any potential impact of this delay on Air Canada's international growth strategy. Air Canada's capital expenditure projections, including the pre-delivery payments, have been amended to reflect this delay. Refer to the table below for Air Canada's current projected planned and committed capital expenditures.

Embraer

By the end of February 2008, the last three ERJ-190 aircraft had been delivered, with a total of 15 Embraer ERJ-175 aircraft and 45 Embraer ERJ-190 aircraft currently in Air Canada's fleet. As at March 31, 2008, 25 options for Embraer ERJ-190 series aircraft remained exercisable. The three firm ERJ-190 aircraft delivered in Quarter 1 2008 were financed through loan commitments from third parties covering approximately 80% of the capital expenditure to be repaid in quarterly instalments for a 12-year term. The loan commitments for two of the three aircraft are based on floating rates at the 90-day US LIBOR plus 1.90% and the loan commitment for one of the three aircraft is based at the fixed rate equivalent of the 90-day US LIBOR plus 1.70%.

Projected Planned and Committed Capital Expenditures

The table below provides Air Canada's current projected planned and committed capital expenditures for the full year 2008, for the next four years and after 2012. Air Canada's capital expenditure projections, including the pre-delivery payments, have been amended to reflect the delay in the deliveries of the Boeing 787 aircraft.

Air Canada Projected planned and committed Capital expenditures ($ millions) (1)(2)	2008	2009	2010	2011	2012	Thereafter
Projected committed expenditures	$ 513	$ 29	$ 53	$ 84	$ 457	$ 3,779
Projected planned but uncommitted expenditures	245	175	169	134	85	
Total projected expenditures	758	204	222	218	542	
Projected financing on committed expenditures	(614)	-	-	-	(404)	
Total projected expenditures, net of financing	**$ 144**	**$ 204**	**$ 222**	**$ 218**	**$ 138**	

(1) *US dollar amounts are converted using the March 31, 2008 noon day rate of 1US$ = Cdn$1.0279. Final aircraft delivery prices include estimated escalation and interest on deferred delivery payments, which is calculated based on the 90-day USD LIBOR rate at March 31, 2008.*

(2) *The dollar amounts reflected above do not include obligations pertaining to day-to-day operations.*

7.5. Air Canada Fleet

Air Canada is implementing its network redesign in the North American market through the increased use of large regional jet aircraft which have lower trip costs than conventional narrowbody aircraft. Air Canada had taken delivery of all 15 Embraer ERJ-175 aircraft by the end of 2006 and had taken delivery of all 45 Embraer ERJ-190 aircraft by the end of February 2008. In order to support the expansion of Air Canada's international operations and reduce unit costs, Air Canada is progressively introducing Boeing 777 aircraft into its fleet. In Quarter 1 2008, three Boeing 777-200LR aircraft and one Boeing 777-300ER aircraft were added to Air Canada's fleet. On April 22, 2008, Air Canada took delivery of one Boeing 777-300 aircraft for a total of 13 Boeing 777 aircraft delivered to date. At the same time as the new aircraft are being added to our fleet, Air Canada is removing older and less efficient aircraft. In Quarter 1 2008, Air Canada took the decision to retire its fleet of Boeing 767-200 aircraft, consisting of 10 aircraft, by the end of 2008. These older aircraft are high unit cost aircraft from both a fuel consumption and maintenance perspective.

Aircraft Interior Refurbishment Program

Air Canada commenced a refurbishment of the interior of its existing aircraft in 2006 in order to offer its customers a world class product. As at May 8, 2008, Air Canada has completed the refurbishment of 35 Airbus A319 aircraft, 34 Airbus A320 aircraft, 10 Airbus A321 aircraft and 23 Boeing 767-300 aircraft to date, for a total of 102 aircraft. Air Canada plans to refurbish an additional 15 aircraft by the end of 2008.

7.6. Capital Management

Each of the ACE and Air Canada Boards of Directors approves the ACE or Air Canada objectives and policies for managing capital as the case may be. Capital management is discussed separately for each entity below.

ACE

ACE views capital as the sum of parent company debt consisting of convertible notes, convertible preferred shares, non-controlling interest and shareholders' equity. This definition of capital used by management may not be comparable to measures presented by other public companies. Capital managed by ACE, summarized from the consolidated statement of financial position, follows:

(Canadian dollars in millions)	March 31, 2008	December 31, 2007
Convertible senior notes	$ 277	$ 273
Convertible preferred shares	188	182
Non-controlling interest	692	757
Shareholders' equity	1,687	3,217
Capital	**$ 2,844**	**$ 4,429**

During Quarter 1 2008, ACE's capital declined $1,585 million to $2,844 million mainly due to the purchase and cancellation of common shares by way of a substantial issuer bid for an aggregate purchase price of $1,498 million (refer to section 4 of this MD&A for additional information).

Air Canada

Air Canada views capital as the sum of long-term debt, non-controlling interest, capitalized operating leases and shareholders' equity. Air Canada currently has pre-delivery financing arranged, and as the aircraft have not yet been delivered, this debt is excluded from the capital base. Air Canada includes capitalized operating leases which is a measure commonly used in the industry to ascribe a value to obligations under operating leases. The value is based on annualized aircraft rent expense multiplied by 7.5 as an estimate of the present value of operating lease obligations, which is a factor commonly used in the airline industry. The measure used may not necessarily reflect the fair value or net present value related to the future minimum lease payments as the measure is not based on the remaining contractual payments and the factor may not recognize discount rates implicit in the actual leases or current rates for similar obligations with similar terms and risks. This definition of capital is used by management and may not be comparable to similar measures presented by other public companies.

Air Canada also monitors its ratio of adjusted net debt to net debt plus equity, with equity defined as shareholders' equity. Adjusted net debt is calculated as the sum of long-term debt, non-controlling interest and capitalized operating leases less cash, cash equivalents and short-term investments.

As at March 31, 2008, Air Canada's capital amounted to $8,550 million ($8,640 million as at December 31, 2007) and the adjusted net debt to net debt plus equity ratio was 68.8% (67.0% as at December 31, 2007). The deterioration from December 31, 2007 in the ratio was attributable, in part, to the net loss recorded in Quarter 1 2008.

7.7. ACE Share Information

At April 30, 2008, the issued and outstanding common shares of ACE, along with common shares potentially issuable, pursuant to convertible preferred shares, convertible senior notes and stock options were as follows:

Number of shares (000)	At April 30, 2008	December 31, 2007
Issued and outstanding common shares		
Class A variable voting shares	40,296	82,229
Class B voting shares	15,838	23,709
Total issued and outstanding common shares	**56,134**	**105,938**
Common shares potentially issuable		
Convertible preferred shares	11,477	11,291
Convertible senior notes	12,600	12,210
Stock options	1,568	1,682
Total common shares potentially issuable	**25,645**	**25,183**
Total outstanding and potentially issuable common shares	**81,779**	**131,121**

On January 10, 2008, ACE accepted for purchase and cancellation a total of 40,023,427 Class A variable voting shares and 9,894,166 Class B voting shares at $30.00 per share for an aggregate purchase price of $1,498 million under the terms of a substantial issuer bid. No convertible preferred shares of ACE were deposited on an as converted basis under the offer.

In connection with the share purchase and cancellation by ACE, the conversion rate of ACE's 4.25% Convertible Senior Notes Due 2035 was adjusted from 37.6879 to 39.0341 Class A variable voting shares or Class B voting shares per $1,000 principal amount of Convertible Senior Notes. The adjustment was effective January 11, 2008 and was determined in accordance with the terms of the indenture governing the Convertible Senior Notes.

8. Related Party Transactions

At March 31, 2008, ACE held a 75% ownership interest in Air Canada. Air Canada has various related party transactions with ACE and other ACE-related entities, including Aeroplan, ACTS Aero and Jazz (up to February 7, 2008). Subsequent to the sale of Jazz units on January 24, 2008 and the termination of the Securityholders' Agreement on February 7, 2008, ACE no longer exercised significant influence over Jazz.

The relationships between Air Canada, Aeroplan, Jazz and ACTS Aero are detailed in ACE's 2007 MD&A dated February 7, 2008. There have been no material changes to related party agreements, including the commercial agreements between Air Canada and Jazz, from what was disclosed at that time.

The related party balances resulting from the application of the related party agreements were as follows:

(Canadian dollars in millions)	March 31, 2008
Accounts receivable	
Aeroplan (Air Canada)	$ 43
Aeroplan - distribution receivable (ACE)	3
ACTS Aero (Air Canada)	119
	$ 165
Accounts payable and accrued liabilities	
ACTS Aero (Air Canada)	$ 94
	$ 94

The Quarter 1 2007 related party revenues and expenses included Aeroplan from March 14 to March 31, 2007. The related party revenues and expenses with Aeroplan and ACTS Aero are summarized as follows:

(Canadian dollars in millions)	Quarter 1 2008
Revenues	
Revenues from Aeroplan related to Aeroplan rewards, net of purchase of Aeroplan miles	$ 40
Property rental revenues from related parties	9
Revenues from corporate services and other	19
	$ 68
Expenses	
Maintenance expense for services from ACTS LP / ACTS Aero	$ 140
Other expenses	4
Recovery of wages, salary and benefit expense for employees assigned to related parties	(81)
	$ 63

In addition to the above revenues and expenses with Jazz, Air Canada transfers fuel inventory and subleases certain aircraft to Jazz on a flow-through basis, which are reported net on Air Canada's statement of operations.

9. Financial Instruments and Risk Management

As described in section 5 of this MD&A, the Corporation adopted CICA sections 3862 and 3863 effective January 1, 2008. These new standards enhance disclosures with respect to financial instruments.

Risk Management
Air Canada is exposed to the following risks as a result of holding financial instruments: interest rate risk, foreign exchange risk, liquidity risk, market risk and fuel risk. The following is a description of these risks and how they are managed.

Interest Rate Risk
Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Air Canada enters into both fixed and floating rate debt and also leases certain assets where the rental amount fluctuates based on changes in short-term interest rates. Air Canada manages interest rate risk on a portfolio basis and seeks financing terms in individual arrangements that are most advantageous taking into account all relevant factors, including credit margin, term and basis. The risk management objective is to minimize the potential for changes in interest rates causing adverse changes in cash flows to Air Canada. The temporary investment portfolio which earns a floating rate of return is an economic hedge for a portion of the floating rate debt.

The ratio of fixed to floating rate debt outstanding is designed to maintain flexibility in Air Canada's capital structure and is based upon a long-term objective of 60% fixed and 40% floating. The current ratio is 66% fixed and 34% floating, including the effects of interest rate swap positions.

The following are the current derivatives employed in interest rate risk management activities and the adjustments recorded in Quarter 1 2008:

- Air Canada's one remaining Embraer ERJ-190 aircraft interest swap contract matured with a fair value of $2 million in favour of the counterparty. No gain or loss was recorded during the period.

- Air Canada recorded a gain of $5 million relating to interest rate swaps pertaining to two Boeing 767 operating leases. These interest rate swaps convert the lease payments on the two aircraft leases from fixed to floating rates.

- Air Canada entered into two cross-currency interest rate swap agreements with terms of March 2019 and May 2019, respectively, relating to Boeing 777 aircraft financing, with an aggregate notional value of $202 million (USD$197 million). These swaps convert US denominated debt principal and interest payments into Canadian denominated debt at a foreign exchange rate of par (US$1/CAD$1) and convert from a fixed rate of 5.208% to a floating rate. These derivative instruments have not been designated as hedges for accounting purposes and are fair-valued on a quarterly basis. As at March 31, 2008, the fair value of these contracts was $6 million in favour of Air Canada.

Foreign Exchange Risk
Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The majority of Air Canada's outstanding debt is denominated in US dollars. The US dollar debt acts as an economic hedge against the related aircraft, which is routinely purchased and sold by Air Canada in US dollars.

Air Canada is also exposed to foreign exchange risk on foreign currency denominated trade receivables and foreign currency denominated net cash flows.

Air Canada's risk management objective is to reduce cash flow risk related to foreign denominated cash flows. To help manage this risk, Air Canada enters into certain foreign exchange forward contracts or currency swaps to manage the risks associated with foreign currency exchange rates. At March 31, 2008, Air Canada had entered into foreign currency forward contracts and option agreements converting US dollars and Euros into Canadian dollars on $1,632 million (US$1,588 million) and $24 million (EUR 15 million) which mature in 2008 and 2009. The fair value of these foreign currency contracts as at March 31, 2008 was $22 million in favour of third parties (December 31, 2007 - $124 million in favour of third parties, $2,132 million (US$2,158 million) and $26 million (EUR 18 million) which mature in 2008 and 2009). During Quarter 1 2008, a gain of $79 million was recorded in foreign exchange gain (loss) related to these derivaties. These derivative instruments have not been designated as hedges for accounting purposes.

The cross-currency swap as described above under interest rate risk acts as an economic hedge of the foreign exchange risk on the financing related to two Boeing 777 aircraft with a principal amount of $202 million (US$197 million) as at March 31, 2008.

Air Canada had also entered into currency swap agreements for 11 CRJ aircraft. These agreements matured in January 2008 with a nominal fair value. No gain or loss was recorded during the period.

Liquidity risk

Liquidity risk is the risk that Air Canada will encounter difficulty in meeting obligations associated with its financial liabilities. The long-term debt issued by Air Canada generally has fixed principal and interest repayment requirements over the term of the instrument.

Air Canada monitors and manages liquidity risk by preparing rolling cash flow forecasts, maintaining flexibility in financing arrangements and having available its $400 million revolving credit facility.

Market Risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: foreign exchange risk, interest rate risk and other price risk, which includes commodity price risk. Refer to the section "Asset-Backed Commercial Paper" below for information regarding these instruments held by Air Canada.

Air Canada is exposed to market risks through the derivative instruments entered into. Air Canada uses derivative instruments only for risk management purposes and not for generating trading profit. As such, any change in cash flows associated with derivative instruments due to their exposure to market risks is designed to be offset by changes in cash flows related to the risk being hedged.

Fuel Price Risk

To manage its exposure to jet fuel prices and minimize volatility in operating cash flows, Air Canada enters into derivative contracts with financial intermediaries.

As at March 31, 2008, Air Canada had hedged 33% of its projected fuel requirement for 2008, 11% of its projected fuel requirement for 2009 and 4% of its fuel requirement for 2010. The remainder of 2008 was hedged at prices that fluctuated between an average of US$103 to US$110 per barrel for jet-fuel based contracts, an average of US$95 to US$98 per barrel for heating oil-based contracts and an average of US$86 to US$95 per barrel for West Texas Intermediate ("WTI") crude-oil based contracts.

Since March 31, 2008, Air Canada has entered into new hedging positions, using swap and costless collar option structures, which have added 4% coverage to the remainder of 2008, 3% coverage to 2009 and 2% coverage to 2010. With these new hedging positions, the remainder of 2008 is hedged at prices that can fluctuate between an average of US$108 to US$116 per barrel for jet-fuel based contracts, an average of US$95 to US$99 per barrel for heating oil-based contracts and an average of US$88 to US$97 per barrel for WTI crude-oil based contracts.

The following information summarizes the financial statement impact of derivatives designated under fuel hedge accounting, before the impact of tax:

- The fair value of outstanding fuel derivatives under hedge accounting at March 31, 2008 was $147 million in favour of Air Canada. At April 30, 2008, the fair value of the outstanding fuel derivatives was $216 million.

- The change in fair value of derivatives during the period was $112 million:

  - The unrealized effective change in the fair value of derivatives recorded in other comprehensive income ("OCI") during Quarter 1 2008 was $134 million before tax expense of $42 million. The realized effective change in the fair value of derivatives recorded in OCI during Quarter 1 2008 was $12 million before tax expense of $4 million. OCI amounts for the three months ended March 31, 2008 are presented net of this tax expense on Air Canada's consolidated statement of comprehensive income.

  - The ineffective change in the fair value of derivative recorded in non-operating income (expense) for Quarter 1 2008 was ($38 million). The ineffective portion is calculated as the difference between the intrinsic value and fair market value of the derivatives as well as the difference between the Air Canada proxy derivative and the counterparty derivative. The increasing amount being recorded in non-operating income (expense) is due to the intrinsic value of the derivatives being higher than the fair market value caused by the rising market price of fuel in comparison to the exercise prices of Air Canada derivatives.

  - The depreciation of the Canadian dollar during Quarter 1 2008 resulted in a foreign exchange gain on fuel derivative contracts of $4 million on USD denominated fuel derivative contracts, which was recorded in foreign exchange gain (loss) on Air Canada's consolidated statement of operations.

- During Quarter 1 2008, hedge accounting was discontinued for certain fuel hedge contracts, with a fair value of $8 million, where the hedging relationship ceased to satisfy the conditions for hedge accounting. The fair value of the contracts that have not settled are now included in derivatives not under hedge accounting. Air Canada continues to hold these derivatives as it believes they continue to be good economic hedges in managing its exposure to jet fuel prices. The value of the accumulated other comprehensive income ("AOCI") balance recognized in connection with these derivatives will be taken into fuel expense upon the maturity of the contracts.

- During Quarter 1 2008, fuel derivative contracts matured with fair values in favour of Air Canada for $32 million. This maturity amount includes $8 million for de-designated contracts.

- During Quarter 1 2008, the benefit to fuel expense was $34 million before tax expense of $11 million. This benefit was recognized through the removal of the amount from AOCI. Included in this amount was $7 million related to the de-designated contracts.

- During Quarter 1 2008, the net impact to AOCI was an increase of $112 million before tax expense of $35 million. As at March 31, 2008, the balance in AOCI was $196 million before tax. The estimated net amount of existing gains and losses reported in AOCI that is expected to be reclassified to net income (loss) during the following 12 months is $172 million before tax.

The following information summarizes the financial statement impact of derivatives not designated under fuel hedge accounting, but held as economic hedges, before the impact of tax:

- During Quarter 1 2008, fuel derivative contracts matured in favour of Air Canada for $7 million.

- The fair value of outstanding fuel derivatives not under hedge accounting at March 31, 2008 was $9 million in favour of Air Canada.

- The change in fair value of the derivative contracts for the period was $6 million and was recorded in non-operating income (expense).

Asset-Backed Commercial Paper ("ABCP")
Air Canada has $37 million ($29 million, net of a fair value adjustment) in non-bank sponsored ABCP which has been recorded in deposits and other assets. These investments were scheduled to mature during Quarter 3 2007. An agreement in principle to restructure the ABCP investments was approved by the Pan-Canadian Committee for Third Party Structured ABCP ("Committee") on December 23, 2007 and approved by vote, which occurred on April 25, 2008. The process is subject to a court hearing as to whether the plan is fair, which is expected in early May 2008. Under the terms of the restructuring, all of the ABCP would be exchanged for longer-term notes that will match the maturity of the underlying assets in the proposed structure. Air Canada is not accruing interest on these investments.

The carrying value as at March 31, 2008 is based on a number of assumptions as to the fair value of the investments including factors such as estimated cash flow scenarios and risk adjusted discount rates. The assumptions used in estimating the fair value of the investments are subject to change, which may result in further adjustments to non-operating results in the future. No adjustment to the carrying value was recorded during Quarter 1 2008.

10. Risk Factors

For a detailed description of the risk factors associated with the Corporation, refer to the section entitled "Risk Factors" in ACE's 2007 annual MD&A dated February 7, 2008. The Corporation is not aware of any significant changes to the Corporation's risk factors from those disclosed at that time. However, the risk factors under Current Legal Proceedings in ACE's 2007 MD&A are revised to provide for the following updates:

The European Commission, the United States Department of Justice and the Competition Bureau in Canada, among other competition authorities, are investigating alleged anti-competitive cargo pricing activities, including the levying of certain fuel surcharges, of a number of airlines and cargo operators, including Air Canada, a number of whom, including Air Canada, have received a statement of objections from the European Commission that sets out the European Commission's preliminary assessment in relation to such matter. Air Canada has provided its reply to the statement of objections. Competition authorities have sought or requested information from Air Canada as part of their investigations. Air Canada is cooperating with these investigations, which are likely to lead to proceedings against Air Canada and a number of airlines and other cargo operators in certain jurisdictions. Air Canada is also named as a defendant in a number of class action lawsuits that have been filed before the United States District Court and in Canada in connection with these allegations.

During Quarter 1 2008, Air Canada recorded a provision of $125 million as a preliminary estimate. This estimate is based upon the current status of the investigations and proceedings and Air Canada's assessment as to the potential outcome for certain of them. This provision does not address the proceedings in all jurisdictions, but only where there is sufficient information to do so. Management has determined it is not possible at this time to predict with any degree of certainty the outcome of all proceedings. Additional material provisions may be required.

The risk factor describing the Air Canada Pilots Association ("ACPA") claim under Current Legal Proceedings is amended to reflect the revised date for the hearing of ACPA's appeal to the Ontario Court of Appeal, now scheduled to be heard on June 27, 2008.

The description of the risk factor related to Regulatory Matters is expanded to reference legislation being considered or enacted by governments (and which may apply to the airline industry), including in relation to carbon emission trading schemes, aimed at reducing carbon emissions.

11. Quarterly Financial Information

The table below describes the Corporation's quarterly financial results for the eight most recent quarters. ACE's results reflect the consolidation of Aeroplan's operations only up to March 14, 2007, the consolidation of Jazz's operations only up to May 24, 2007 and ACTS' operations only up to October 16, 2007. After those dates, ACE's investments in Aeroplan, ACTS Aero and Jazz (from May 24, 2007 to February 7, 2008) are accounted for using the equity method. The equity income from ACE's investment in Aeroplan, ACTS Aero and Jazz (up to February 7, 2008) is recorded in non-operating income (expense) on ACE's consolidated statement of operations. Effective February 7, 2008, ACE's investment in Jazz is classified as an available-for-sale investment and distributions from Jazz Air Income Fund are also recorded in non-operating expense income (expense) on ACE's consolidated statement of operations.

($ millions, except per share amounts)	Q2 2006	Q3 2006	Q4 2006	Q1 2007[2]	Q2 2007[3]	Q3 2007	Q4 2007[4]	Q1 2008
Operating revenues	$ 2,682	$ 2,947	$ 2,544	$ 2,625	$ 2,659	$ 3,022	$ 2,520	$ 2,726
Special charge for Aeroplan miles[1]	-	(102)	-	-	-	-	-	-
Operating revenues	**2,682**	**2,845**	**2,544**	**2,625**	**2,659**	**3,022**	**2,520**	**2,726**
Operating expenses	(2,501)	(2,642)	(2,471)	(2,654)	(2,563)	(2,682)	(2,474)	(2,753)
Operating income (loss) before under-noted item[5]	**181**	**203**	**73**	**(29)**	**96**	**340**	**46**	**(27)**
Provision for cargo investigations[6]	-	-	-	-	-	-	-	(125)
Operating income (loss)	**181**	**203**	**73**	**(29)**	**96**	**340**	**46**	**(152)**
Total non-operating income (expense), non-controlling interest, foreign exchange gain (loss) and income tax[7]	55	(100)	(122)	(43)	22	(116)	1,082	(30)
Net income (loss)	**$ 236**	**$ 103**	**$ (49)**	**$ (72)**	**$ 118**	**$ 224**	**$ 1,128**	**$ (182)**
Earning (loss)[8]								
Per share – basic	**$ 2.32**	**$ 1.01**	**$ (0.48)**	**$ (0.70)**	**$ 1.14**	**$ 2.17**	**$ 10.81**	**$ (2.96)**
Per share – diluted	**$ 2.05**	**$ 0.95**	**$ (0.48)**	**$ (0.70)**	**$ 0.98**	**$ 1.84**	**$ 8.88**	**$ (2.96)**

(1) *Quarter 3 2006 includes a special charge of $102 million in connection with Air Canada's obligations for the redemption of pre-2002 Aeroplan miles.*
(2) *ACE ceased consolidating Aeroplan's results effective March 14, 2007.*
(3) *ACE ceased consolidating Jazz's results effective May 24, 2007.*
(4) *ACE ceased consolidating ACTS' results effective October 16, 2007.*
(5) *Quarter 1 2007 and Quarter 2 2007 include special charges for labour restructuring of $9 million and $6 million, respectively.*
(6) *Air Canada recorded a provision for cargo investigations of $125 million in Quarter 1 2008.*
(7) *Quarter 2 2006 includes a gain of $100 million and a tax provision of $17 million relating to the sale of 3.25 million shares of its holdings in US Airways. Quarter 3 2006 includes a gain of $52 million and a tax provision of $9 million relating to the sale of 1.25 million shares of its holdings in US Airways. Quarter 4 2006 includes a dilution gain of $25 million and a tax expense of $4 million related to the Air Canada initial public offering. Quarter 2 2007 includes a gain of $4 million and a tax provision of $1 million relating to the sale of 0.249 million shares of its holdings in US Airways. Quarter 3 2007 includes a gain of $4 million and a tax provision of $1 million relating to the sale of 0.251 million shares of its holdings in US Airways. Quarter 4 2007 includes an aggregate gain on disposal of $1,339 million and a tax provision of $214 million mainly comprised of a gain on disposal of $565 million and a tax provision of $82 million related to the monetization of ACTS which was completed on October 16, 2007, a gain on disposal of $539 million and a tax provision of $91 million related to the secondary offering of 22,000,000 trust units of Aeroplan Income Fund and a gain on disposal of $233 million and a tax provision of $41 million related to the secondary offering of 35,500,000 trust units of Jazz Air Income Fund. Quarter 1 2008 includes a gain of $89 million ($71 million, net of tax) on ACE's sale of 13,000,000 units of Jazz Air Income Fund and an impairment provision of $38 million ($26 million, net of tax) recorded by Air Canada related to its fleet of Boeing 767-200 aircraft.*
(8) *Loss per share for Quarter 1 2008 includes the impact of the substantial issuer bid completed by ACE on January 10, 2008 whereby ACE accepted for purchase and cancellation a total of 40,023,427 Class A variable voting shares and 9,894,166 Class B voting shares.*

12. Off-Balance Sheet Arrangements

There were no significant changes to ACE's off-balance sheet arrangements from what was disclosed in ACE's 2007 MD&A dated February 7, 2008.

13. Controls and Procedures

Disclosure Controls and Procedures

Disclosure controls and procedures within ACE are designed to provide reasonable assurance that all relevant information is identified to its Disclosure Policy Committee to ensure appropriate and timely decisions are made regarding public disclosure.

ACE's 2007 Annual Report contains a statement that the Chairman, President and Chief Executive Officer and the Executive Vice President and Chief Financial Officer have concluded that ACE's disclosure controls and procedures are effective based upon an evaluation of these controls and procedures conducted at December 31, 2007.

Changes in Internal Controls over Financial Reporting

There were no changes to ACE's internal controls over financial reporting during the three months ended March 31, 2008 that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

14. Subsequent Events

Disposal of Aeroplan Income Fund Units

On April 21, 2008 ACE completed the sale of a total of 20,400,000 trust units of Aeroplan Income Fund at a price of $17.50 per unit representing total net proceeds to ACE of approximately $343 million. Immediately following the sale, ACE held approximately 9.9% of the issued and outstanding units of Aeroplan Income Fund.

15. Non-GAAP Financial Measures

EBITDAR/EBITDA

EBITDAR (earnings before interest, taxes, depreciation, amortization, obsolescence and aircraft rent) is a non-GAAP financial measure commonly used in the airline industry to view operating results before aircraft rent, depreciation, obsolescence and amortization, as these costs can vary significantly among airlines due to differences in the way airlines finance their aircraft and other assets. For businesses without aircraft rent, such as Aeroplan and ACTS, EBITDA (earnings before interest, taxes, depreciation, amortization and obsolescence) is used to view operating results before depreciation, amortization and obsolescence, as these costs can vary significantly among companies due to differences in the way companies finance their assets. Management considers that the provision for cargo investigations is not reflective of the underlying financial performance of Air Canada from ongoing operations. The Corporation excludes this item as it could potentially distort the analysis of trends in business performance.

EBITDAR and EBITDA are not recognized measures for financial statement presentation under GAAP and do not have a standardized meaning and are therefore not likely to be comparable to similar measures presented by other public companies. **ACE's EBITDAR for Quarter 1 2008 is not directly comparable to its EBITDAR for Quarter 1 2007. Refer to section 5 of this MD&A for additional information.**

EBITDAR before the provision for cargo investigations and EBITDA and EBITDAR are reconciled to operating income (loss) as follows:

(Canadian dollars in millions)	Quarter 1 2008	Quarter 1 2007	$ Change
Air Canada			
GAAP operating loss before provision for cargo investigations	$ (12)	$ (78)	$ 66
Add back:			
Aircraft rent	63	79	(16)
Depreciation and amortization	171	128	43
EBITDAR before provision for cargo investigations	**222**	**129**	**93**
Provision for cargo investigations	(125)	-	(125)
EBITDAR	**$ 97**	**$ 129**	**$ (32)**
Aeroplan[1][2]			
GAAP operating income	$ -	$ 40	$ (40)
Add back:			
Depreciation and amortization	-	3	(3)
EBITDA	**$ -**	**$ 43**	**$ (43)**
Jazz[2]			
GAAP operating income	$ -	$ 36	$ (36)
Add back:			
Aircraft rent	-	35	(35)
Depreciation and amortization	-	5	(5)
EBITDAR	**$ -**	**$ 76**	**$ (76)**
ACTS[2]			
GAAP operating income	$ -	$ 3	$ (3)
Add back:			
Depreciation and amortization	-	9	(9)
EBITDA	**$ -**	**$ 12**	**$ (12)**
ACE Consolidated[2]			
GAAP operating loss before provision for cargo investigations	$ (27)	$ (29)	$ 2
Add back:			
Aircraft rent	63	104	(41)
Depreciation, amortization and obsolescence	169	146	23
EBITDAR before provision for cargo investigations	**205**	**221**	**(16)**
Provision for cargo investigations	(125)	-	(125)
EBITDAR	**$ 80**	**$ 221**	**$ (141)**

(1) The information above reflects Aeroplan's results from January 1 to March 13, 2007.
(2) ACE ceased consolidating Aeroplan's, Jazz's and ACTS' results effective March 14, 2007, May 24, 2007 and October 16, 2007, respectively.

16. Glossary of Terms

Available Seat Miles or ASMs — A measure of passenger capacity calculated by multiplying the total number of seats available for passengers by the miles flown;

CASM — Operating expense per ASM;

EBITDA — EBITDA is earnings before interest, taxes, depreciation, amortization and obsolescence and is a non-GAAP financial measure;

EBITDAR — EBITDAR is earnings before interest, taxes, depreciation, amortization, obsolescence and aircraft rent and is a non-GAAP financial measure;

Passenger Load Factor — A measure of passenger capacity utilization derived by expressing Revenue Passenger Miles as a percentage of Available Seat Miles;

Passenger Revenue per Available Seat Mile or RASM — Average passenger revenue per ASM;

Revenue Passenger Miles or RPMs — A measure of passenger traffic calculated by multiplying the total number of revenue passengers carried by the miles they are carried;

Yield — Average passenger revenue per RPM.