

Aircastle LTD  
Form 10-Q  
August 07, 2009

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**  
For the quarterly period ended **June 30, 2009**

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
**Commission File number 001-32959**  
**AIRCASTLE LIMITED**  
(Exact name of registrant as specified in its charter)

**Bermuda**  
(State or other jurisdiction of incorporation or  
organization)

**98-0444035**  
(IRS Employer Identification No.)

**c/o Aircastle Advisor LLC**  
**300 First Stamford Place, 5<sup>th</sup> Floor,**  
**Stamford, CT**

(Address of principal executive offices)

**06902**  
(Zip Code)

Registrant's telephone number, including area code **(203) 504-1020**

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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

As of July 31, 2009, there were 79,234,663 outstanding shares of the registrant's common shares, par value \$0.01 per share.

**Aircastle Limited and Subsidiaries  
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**Aircastle Limited and Subsidiaries**  
**Consolidated Balance Sheets**  
(Dollars in thousands, except share data)

|   | <b>December<br/>31,<br/>2008</b> | <b>June 30,<br/>2009<br/>(Unaudited)</b> |
|---|----------------------------------|--|
| <b>ASSETS</b>   |                                  |  |
| Cash and cash equivalents   | \$ 80,947                        | \$ 95,785                                |
| Accounts receivable   | 3,161                            | 5,597                                    |
| Debt investments  | 14,349                           | 13,691                                   |
| Restricted cash and cash equivalents  | 182,623                          | 199,377                                  |
| Restricted liquidity facility collateral  |                                  | 81,186                                   |
| Flight equipment held for lease, net of accumulated depreciation of \$371,591 and \$474,350   | 3,837,543                        | 3,832,039                                |
| Aircraft purchase deposits and progress payments  | 68,923                           | 107,357                                  |
| Leasehold improvements, furnishings and equipment, net of accumulated depreciation of \$1,999 and \$2,240   | 1,174                            | 1,016                                    |
| Other assets  | 62,852                           | 82,648                                   |
| Total assets  | \$ 4,251,572                     | \$ 4,418,696                             |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>  |                                  |  |
| <b>LIABILITIES</b>  |                                  |  |
| Borrowings from securitizations and term debt financings  | \$ 2,476,296                     | \$ 2,481,365                             |
| Accounts payable, accrued expenses and other liabilities  | 60,789                           | 62,269                                   |
| Dividends payable   | 7,862                            | 7,923                                    |
| Lease rentals received in advance   | 28,463                           | 27,235                                   |
| Liquidity facility  |                                  | 81,186                                   |
| Security deposits   | 65,307                           | 94,837                                   |
| Maintenance payments  | 224,288                          | 241,074                                  |
| Fair value of derivative liabilities  | 276,401                          | 191,411                                  |
| Total liabilities   | 3,139,406                        | 3,187,300                                |
| Commitments and Contingencies   |                                  |  |
| <b>SHAREHOLDERS EQUITY</b>  |                                  |  |
| Preference shares, \$.01 par value, 50,000,000 shares authorized, no shares issued and outstanding  |                                  |  |
| Common shares, \$.01 par value, 250,000,000 shares authorized, 78,620,320 shares issued and outstanding at December 31, 2008; and 79,234,663 shares issued and outstanding at June 30, 2009 | 786                              | 792                                      |
| Additional paid-in capital  | 1,474,455                        | 1,476,533                                |

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|  |              |              |
|--|--------------|--------------|
| Retained earnings (deficit)                | (473)        | 29,723       |
| Accumulated other comprehensive loss       | (362,602)    | (275,652)    |
| Total shareholders' equity                 | 1,112,166    | 1,231,396    |
| Total liabilities and shareholders' equity | \$ 4,251,572 | \$ 4,418,696 |

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

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

|   | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |             |
|---|---------------------------|-------------|-------------------------|-------------|
|   | <b>June 30,</b>           |             | <b>June 30,</b>         |             |
|   | <b>2008</b>               | <b>2009</b> | <b>2008</b>             | <b>2009</b> |
| <b>Revenues:</b>  |                           |             |                         |             |
| Lease rental revenue  | \$ 137,647                | \$ 129,406  | \$ 268,628              | \$ 255,400  |
| Amortization of net lease discounts and lease incentives  | 2,502                     | (2,810)     | 5,148                   | (3,927)     |
| Maintenance revenue   | 4,142                     | 9,637       | 4,142                   | 16,240      |
| <br>  |                           |             |                         |             |
| Total lease rentals   | 144,291                   | 136,233     | 277,918                 | 267,713     |
| Interest income   | 614                       | 594         | 1,905                   | 1,227       |
| Other revenue   | 490                       | 86          | 528                     | 111         |
| <br>  |                           |             |                         |             |
| Total revenues  | 145,395                   | 136,913     | 280,351                 | 269,051     |
| <br>  |                           |             |                         |             |
| <b>Expenses:</b>  |                           |             |                         |             |
| Depreciation  | 51,605                    | 51,688      | 99,820                  | 103,249     |
| Interest, net   | 51,319                    | 41,482      | 92,330                  | 84,893      |
| Selling, general and administrative (including non-cash share based payment expense of \$1,615 and \$1,729 for the three months ended, and \$3,213 and \$3,387 for the six months ended June 30, 2008 and 2009, respectively) | 11,354                    | 11,122      | 22,843                  | 22,217      |
| Maintenance and other costs   | 597                       | 4,502       | 1,242                   | 10,278      |
| <br>  |                           |             |                         |             |
| Total expenses  | 114,875                   | 108,794     | 216,235                 | 220,637     |
| <br>  |                           |             |                         |             |
| <b>Other income:</b>  |                           |             |                         |             |
| Gain on sale of aircraft  | 5,126                     |             | 5,126                   |             |
| Other   | 1,328                     | 1,501       | 1,083                   | 1,593       |
| <br>  |                           |             |                         |             |
| Total other income  | 6,454                     | 1,501       | 6,209                   | 1,593       |
| <br>  |                           |             |                         |             |
| Income from continuing operations before income taxes   | 36,974                    | 29,620      | 70,325                  | 50,007      |
| Income tax provision  | 1,633                     | 2,049       | 3,347                   | 3,965       |
| <br>  |                           |             |                         |             |
| Net income  | \$ 35,341                 | \$ 27,571   | \$ 66,978               | \$ 46,042   |
| <br>  |                           |             |                         |             |
| Earnings per common share Basic   | \$ 0.45                   | \$ 0.35     | \$ 0.85                 | \$ 0.58     |

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|                              |         |         |         |         |         |
|------------------------------|---------|---------|---------|---------|---------|
| Earnings per common share    | Diluted | \$ 0.45 | \$ 0.35 | \$ 0.85 | \$ 0.58 |
| Dividends declared per share |         | \$ 0.25 | \$ 0.10 | \$ 0.50 | \$ 0.20 |

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

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

|   | <b>Six Months Ended</b> |             |
|---|-------------------------|-------------|
|   | <b>June 30,</b>         |             |
|   | <b>2008</b>             | <b>2009</b> |
| <b>Cash flows from operating activities:</b>                                      |                         |             |
| Net income  | \$ 66,978               | \$ 46,042   |
| Adjustments to reconcile net income to net cash provided by operating activities: |                         |             |
| Depreciation  | 99,820                  | 103,249     |
| Amortization of deferred financing costs  | 6,787                   | 5,731       |
| Amortization of net lease discounts and lease incentives                          | (5,148)                 | 3,927       |
| Deferred income taxes   | 2,604                   | 3,348       |
| Accretion of purchase discounts on debt investments                               | (277)                   | (288)       |
| Non-cash share based payment expense  | 3,213                   | 3,387       |
| Cash flow hedges reclassified into earnings                                       | 530                     | 10,554      |
| Ineffective portion of cash flow hedges   | 5,905                   | (3,331)     |
| Gain on sale of flight equipment  | (5,126)                 |             |
| Security deposits and maintenance payments included in earnings                   | (3,322)                 | (10,506)    |
| Loss on sale of investments   | 245                     |             |
| Other   | (731)                   | (1,164)     |
| Changes in certain assets and liabilities:  |                         |             |
| Accounts receivable   | (1,731)                 | (2,281)     |
| Restricted cash and cash equivalents  | (26,686)                | (16,754)    |
| Other assets  | 1,210                   | (4,077)     |
| Accounts payable, accrued expenses and other liabilities                          | (2,773)                 | (10,118)    |
| Payable to affiliates   | (200)                   |             |
| Lease rentals received in advance   | (4,110)                 | (1,228)     |
| Net cash provided by operating activities   | 137,188                 | 126,491     |
| <b>Cash flows from investing activities:</b>                                      |                         |             |
| Acquisition and improvement of flight equipment and lease incentives              | (221,310)               | (105,746)   |
| Aircraft purchase deposits and progress payments, net of returned deposits        | 8,974                   | (39,715)    |
| Proceeds from sale of flight equipment  | 21,366                  |             |
| Proceeds from sale of debt investments  | 65,335                  |             |
| Principal repayments on debt investments  | 11,467                  | 808         |
| Collateral call payments on derivatives and repurchase agreements                 | (296,605)               |             |
| Collateral call receipts on derivatives and repurchase agreements                 | 330,943                 |             |
| Leasehold improvements, furnishings and equipment                                 | (334)                   | (82)        |
| Net cash used in investing activities   | (80,164)                | (144,735)   |
| <b>Cash flows from financing activities:</b>                                      |                         |             |
| Issuance, net of repurchases, of common shares to directors and employees         | (1,263)                 | (247)       |



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|  |             |           |
|--|-------------|-----------|
| Proceeds from term debt financings   | 786,135     | 70,916    |
| Securitization and term debt financing repayments  | (49,504)    | (65,847)  |
| Restricted cash and cash equivalents related to unreleased securitization and credit facility borrowings | (138)       |           |
| Deferred financing costs   | (17,568)    | (3,098)   |
| Credit facility borrowings   | 482,723     |           |
| Credit facility repayments   | (1,025,720) |           |
| Principal repayments on repurchase agreements  | (67,744)    |           |
| Security deposits and maintenance payments received  | 56,498      | 70,695    |
| Security deposits and maintenance payments returned  | (14,066)    | (20,794)  |
| Payments for terminated cash flow hedges   | (68,332)    | (2,758)   |
| Dividends paid   | (74,644)    | (15,785)  |
| Net cash provided by financing activities  | 6,377       | 33,082    |
| <b>Net increase in cash and cash equivalents</b>   | 63,401      | 14,838    |
| Cash and cash equivalents at beginning of period   | 13,546      | 80,947    |
| Cash and cash equivalents at end of period   | \$ 76,947   | \$ 95,785 |
| <b>Supplemental disclosures of cash flow information:</b>  |             |           |
| Cash paid for interest, net of capitalized interest  | \$ 81,334   | \$ 73,428 |
| Cash paid for income taxes   | \$ 1,594    | \$ 1,568  |

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

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**Aircastle Limited and Subsidiaries**  
**Notes to Unaudited Consolidated Financial Statements**  
**(Dollars in thousands, except per share amounts)**  
**June 30, 2009**

**Note 1. Summary of Significant Accounting Policies**

**Organization**

Aircastle Limited ( Aircastle, the Company, we, us or our ) is a Bermuda exempted company that was incorporated on October 29, 2004 by Fortress Investment Group LLC and certain of its affiliates (together, the Fortress Shareholders or Fortress ) under the provisions of Section 14 of the Companies Act of 1981 of Bermuda. Aircastle's business is investing in aviation assets, including leasing, managing and selling commercial jet aircraft to airlines throughout the world and in aircraft related debt investments.

**Basis of Presentation**

Aircastle is a holding company that conducts its business through subsidiaries. Aircastle directly or indirectly owns all of the outstanding common shares of its subsidiaries. The consolidated financial statements presented are prepared in accordance with U.S. generally accepted accounting principles ( GAAP ). We operate in a single segment.

The accompanying consolidated financial statements are unaudited and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC ) for interim financial reporting and, in our opinion, reflect all adjustments, including normal recurring items, which are necessary to present fairly the results for interim periods. Operating results for the periods presented are not necessarily indicative of the results that may be expected for the entire year. Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with GAAP have been omitted in accordance with the rules and regulations of the SEC; however, we believe that the disclosures are adequate to make information presented not misleading. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2008. The Company's management has reviewed and evaluated all events or transactions for potential recognition and/or disclosure since the balance sheet date of June 30, 2009 through August 7, 2009, the date on which the consolidated financial statements included in this Form 10-Q were issued.

Effective January 1, 2009, the Company adopted Financial Accounting Standards Board ( FASB ) Statement of Accounting Standards ( SFAS ) No. 161, *Disclosures about Derivative Instruments and Hedging Activities*, an amendment of FASB Statement No. 133 *Accounting for Derivative Instruments and Hedging Activities*, ( SFAS No. 161 ). SFAS No. 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. See Note 10 Derivatives.

Also effective January 1, 2009, the Company adopted FASB Staff Position ( FSP ) No. EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* ( FSP No. EITF 03-6-1 ). FSP No. EITF 03-6-1 addresses whether unvested share-based payment awards with rights to receive dividends or dividend equivalents should be considered participating securities for the purposes of applying the two-class method of calculating earnings per share ( EPS ) under SFAS No. 128, *Earnings per Share*. The FASB staff concluded that unvested share-based payment awards that contain rights to receive nonforfeitable dividends or dividend equivalents (whether paid or unpaid) are participating securities and thus should be included in the two-class method of computing EPS. The adoption of FSP No. EITF 03-6-1 requires us to present EPS using the two-class method for our current period EPS computations and to retrospectively revise our comparative prior period EPS computations using the two-class method. The adoption of FSP No. EITF 03-6-1 did not have a material effect on EPS. See Note 6 Earnings Per Share.

**Principles of Consolidation**

The consolidated financial statements include the accounts of Aircastle and all of its subsidiaries. Aircastle consolidates four Variable Interest Entities ( VIEs ) in accordance with FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* ( FIN 46 ) of which Aircastle is the primary beneficiary. All intercompany transactions and balances have been eliminated in consolidation.



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**Aircastle Limited and Subsidiaries**  
**Notes to Unaudited Consolidated Financial Statements**  
**(Dollars in thousands, except per share amounts)**  
**June 30, 2009**

**Recent Accounting Pronouncements**

In April, 2009, the FASB issued three final FSPs intended to provide additional application guidance and enhance disclosures regarding fair value measurements and impairments of securities. FSP No. FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, provides guidelines for making fair value measurements more consistent with the principles presented in FASB Statement No. 157, *Fair Value Measurements*. FSP No. FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*, enhances consistency in financial reporting by increasing the frequency of fair value disclosures. FSP FAS 115-2, FAS 124-2 and EITF 99-20-2, *Recognition and Presentation of Other-Than-Temporary Impairments*, provides additional guidance designed to create greater clarity and consistency in accounting for and presenting impairment losses on securities. The FSPs are effective for interim and annual periods ending after June 15, 2009. The Company adopted these FSPs during the second quarter of 2009 and the adoption of these FSPs did not have a material impact on our consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, *Subsequent Events* ( SFAS No. 165 ). SFAS No. 165 is intended to establish general standards of accounting for, and disclosure of, events that occur after the balance sheet date but before financial statements are issued or are available to be issued. It requires the disclosure of the date through which an entity has evaluated subsequent events and the basis for that date that is, whether that date represents the date the financial statements were issued or were available to be issued. SFAS No. 165 is effective for interim and annual periods ending after June 15, 2009. The Company adopted SFAS No. 165 during the second quarter of 2009 and the adoption of SFAS No. 165 did not have a material impact on our consolidated financial statements.

In June 2009, the FASB issued SFAS No. 167, *Amendments to FASB Interpretation ( FIN ) No. 46(R)* ( SFAS No. 167 ), which amends FIN No. 46(R) to require an enterprise to perform an analysis to determine whether the enterprise's variable interest, or interests, give it a controlling financial interest in a variable interest entity. The determination of whether a reporting entity is required to consolidate another entity is based on, among other things, the other entity's purpose and design and the reporting entity's ability to direct the activities of the other entity that most significantly impact the other entity's economic performance. This Statement amends certain guidance in FIN No. 46(R) for determining whether an entity is a variable interest entity and requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity. SFAS No. 167 will require a reporting entity to provide additional disclosures about its involvement with variable interest entities and any significant changes in risk exposure due to that involvement. SFAS No. 167 will be effective for fiscal years beginning after November 15, 2009, and interim periods within those fiscal years. The Company is currently evaluating the requirements of SFAS No. 167 and has not yet determined the impact on the Company's consolidated financial statements.

Also in June 2009, the FASB issued SFAS No. 168, *The FASB Accounting Standards Codification<sup>TM</sup>* ( Codification ) and the *Hierarchy of Generally Accepted Accounting Principles, a replacement of FASB Statement No. 162* ( SFAS No. 168 ). This Statement replaces FASB Statement No. 162, *The Hierarchy of Generally Accepted Accounting Principles* and identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP in the United States (the GAAP hierarchy). Rules and interpretive releases of the SEC under federal securities laws are also sources of authoritative GAAP for SEC registrants. The Codification does not replace or affect guidance issued by the SEC or its staff for public entities in their filings with the SEC. SFAS No. 168 shall be effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Company plans to adopt SFAS No. 168 during the third quarter of 2009 and the adoption of SFAS No. 168 is not expected to have a material effect on our consolidated financial statements.

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**Notes to Unaudited Consolidated Financial Statements**  
**(Dollars in thousands, except per share amounts)**  
**June 30, 2009**

**Note 2. Fair Value Measurements**

SFAS No. 157, *Fair Value Measurements*, requires the use of valuation techniques to measure fair value that maximize the use of observable inputs and minimize use of unobservable inputs. These inputs are prioritized as follows:

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

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

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

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

**Market approach** Uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

**Income approach** Uses valuation techniques to convert future amounts to a single present amount based on current market expectation about those future amounts.

**Cost approach** Based on the amount that currently would be required to replace the service capacity of an asset (replacement cost).

The following table sets forth our financial assets and liabilities as of June 30, 2009 that we measured at fair value on a recurring basis by level within the fair value hierarchy. As required by SFAS No. 157, assets and liabilities measured at fair value are classified in their entirety based on the lowest level of input that is significant to their fair value measurement.

|                                      | Fair Value<br>as of<br>June 30,<br>2009 | Fair Value Measurements at June 30, 2009<br>Using Fair Value Hierarchy |            |           | Valuation<br>Technique |
|--------------------------------------|---|--|------------|-----------|------------------------|
|                                      |   | Level 1  | Level 2    | Level 3   |                        |
| <b>Assets:</b>                       |   |  |            |           |                        |
| Cash and cash equivalents            | \$ 95,785                               | \$ 95,785  | \$         | \$        | Market                 |
| Restricted cash and cash equivalents | 199,377                                 | 199,377  |            |           | Market                 |
| Debt investments                     | 13,691                                  |  |            | 13,691    | Income                 |
| Total                                | \$ 308,853                              | \$ 295,162   | \$         | \$ 13,691 |                        |
| <b>Liabilities:</b>                  |   |  |            |           |                        |
| Derivative liabilities               | \$ 191,411                              | \$   | \$ 152,571 | \$ 38,840 | Income                 |

Our cash and cash equivalents, along with our restricted cash and cash equivalents balances, consist largely of money market securities that are considered to be highly liquid and easily tradable. These securities are valued using inputs observable in active markets for identical securities and are therefore classified as level 1 within our fair value hierarchy. Our interest rate derivatives included in level 2 consist of United States dollar denominated interest rate swaps, and their fair values are determined by applying standard modeling techniques under the income approach to

relevant market interest rates (cash rates, futures rates, swap rates) in effect at the period close to determine appropriate reset and discount rates.

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**Aircastle Limited and Subsidiaries**  
**Notes to Unaudited Consolidated Financial Statements**  
**(Dollars in thousands, except per share amounts)**  
**June 30, 2009**

Our debt investments included in Level 3 consist of available-for-sale United States corporate obligations consisting of interests in pools of loans which are collateralized by interests in commercial aircraft. The fair value of our debt investments included within Level 3 is valued by using discounted cash flow methodologies, where the inputs to those models are based on unobservable market inputs. The Company used two sources of unobservable inputs; we obtained broker quotes which provided an indication of the market value and we obtained market values from a pricing service. We used the broker quotes and/or the pricing service market values to validate the discount rate used for our cash flow model for these debt investments in accordance with SFAS 157-3.

Our interest rate derivatives included in Level 3 consist of United States dollar denominated interest rate swaps with a guaranteed notional balance. The guaranteed notional balance has an upper notional band that matches the hedged debt and a lower notional band. The notional balance is guaranteed to match the hedged debt balance if the debt balances decreases within the upper and lower notional band. The fair value of the interest rate derivative is determined based on the upper notional band using cash flows discounted at the relevant market interest rates in effect at the period close. The range of the guaranteed notional between the upper and lower band represents an option that may not be exercised independently of the debt notional and is therefore valued based on unobservable market inputs.

The following tables reflect the activity for the major classes of our assets and liabilities measured at fair value using level 3 inputs for the three and six months ended June 30, 2009:

|  | <b>Three Months Ended</b> |                    | <b>Six Months Ended</b> |                    |
|--|---------------------------|--------------------|-------------------------|--------------------|
|  | <b>June 30, 2009</b>      |                    | <b>June 30, 2009</b>    |                    |
|  | <b>Assets</b>             | <b>Liabilities</b> | <b>Assets</b>           | <b>Liabilities</b> |
|  | <b>Debt</b>               | <b>Derivative</b>  | <b>Debt</b>             | <b>Derivative</b>  |
|  | <b>Investments</b>        | <b>Liabilities</b> | <b>Investments</b>      | <b>Liabilities</b> |
| Balance at beginning of period         | \$ 12,626                 | \$ (62,327)        | \$ 14,349               | \$ (66,321)        |
| Transfers in (out)                     |                           |                    |                         |                    |
| Principal repayments                   | (1)                       |                    | (808)                   |                    |
| Total gains/(losses), net:             |                           |                    |                         |                    |
| Included in interest income            | 130                       |                    | 288                     |                    |
| Included in other income (expense)     |                           | (146)              |                         | (295)              |
| Included in interest expense           |                           | (65)               |                         | (123)              |
| Included in other comprehensive income | 936                       | 23,698             | (138)                   | 27,899             |
| Balance at end of period               | \$ 13,691                 | \$ (38,840)        | \$ 13,691               | \$ (38,840)        |

There were no assets and liabilities measured at fair value on a non-recurring basis.

Our financial instruments, other than cash, consist principally of cash equivalents, restricted cash and cash equivalents, accounts receivable, debt investments, accounts payable, amounts borrowed under financings and interest rate derivatives. The fair value of cash, cash equivalents, restricted cash and cash equivalents, accounts receivable and accounts payable approximates the carrying value of these financial instruments because of their short term nature.

The fair values of our securitizations which contain third-party credit enhancements are estimated using a discounted cash flow analysis, based on our current incremental borrowing rates of borrowing arrangements that do not contain third-party credit enhancements. The fair values of our term debt financings are estimated using a discounted cash flow analysis, based on our current incremental borrowing rates for similar types of borrowing arrangements.

The carrying amounts and fair values of our financial instruments at December 31, 2008 and June 30, 2009 are as follows:

|   | <b>December 31, 2008</b>                                |  | <b>June 30, 2009</b>                                    |  |
|---|---|--|---|--|
|   | <b>Carrying<br/>Amount<br/>of Asset<br/>(Liability)</b> | <b>Fair Value<br/>of Asset<br/>(Liability)</b> | <b>Carrying<br/>Amount<br/>of Asset<br/>(Liability)</b> | <b>Fair Value<br/>of Asset<br/>(Liability)</b> |
| Debt investments                            | \$ 14,349   | \$ 14,349                                      | \$ 13,691   | \$ 13,691                                      |
| Securitizations and term debt<br>financings | (2,476,296)   | (2,328,574)                                    | (2,410,822)   | (2,065,329)                                    |
| ECA term financing                          |   |  | (70,543)  | (70,543)                                       |
| Derivative liabilities                      | (276,401)   | (276,401)                                      | (191,411)   | (191,411)                                      |

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

The contracted minimum future lease rental payments to be received under our existing operating leases at June 30, 2009 were as follows:

| <b>Year Ending December 31,</b> | <b>Amount</b>       |
|---------------------------------|---------------------|
| Remainder of 2009               | \$ 253,840          |
| 2010                            | 467,870             |
| 2011                            | 419,401             |
| 2012                            | 363,090             |
| 2013                            | 267,443             |
| 2014                            | 200,278             |
| Thereafter                      | 419,494             |
| <b>Total</b>                    | <b>\$ 2,391,416</b> |

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

| <b>Region</b>          | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |             |
|------------------------|---------------------------|-------------|-------------------------|-------------|
|                        | <b>June 30,</b>           |             | <b>June 30,</b>         |             |
|                        | <b>2008</b>               | <b>2009</b> | <b>2008</b>             | <b>2009</b> |
| Europe                 | 45%                       | 46%         | 45%                     | 46%         |
| Asia                   | 24%                       | 20%         | 25%                     | 21%         |
| North America          | 12%                       | 16%         | 12%                     | 16%         |
| Latin America          | 9%                        | 7%          | 8%                      | 6%          |
| Middle East and Africa | 10%                       | 11%         | 10%                     | 11%         |
| <b>Total</b>           | <b>100%</b>               | <b>100%</b> | <b>100%</b>             | <b>100%</b> |

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

For the three months ended June 30, 2008, one customer accounted for 8% of lease rental revenue and four additional customers accounted for a combined 21% of lease rental revenue. No other customer accounted for more than 4% of lease rental revenue. For the three months ended June 30, 2009, one customer accounted for 9% of lease rental revenue and three additional customers accounted for a combined 17% of lease rental revenue. No other customer accounted for more than 4% of lease rental revenue.

For the six months ended June 30, 2008, one customer accounted for 8% of lease rental revenue and four additional customers accounted for a combined 20% of lease rental revenue. No other customer accounted for more than 4% of lease rental revenue. For the six months ended June 30, 2009, one customer accounted for 9% of lease rental revenue and three additional customers accounted for a combined 17% of lease rental revenue. No other customer accounted for more than 4% of lease rental revenue.

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Geographic concentration of net book value of flight equipment held for lease was as follows:

| <b>Region</b>          | <b>December 31, 2008</b>          |                             | <b>June 30, 2009</b>              |                             |
|------------------------|-----------------------------------|-----------------------------|-----------------------------------|-----------------------------|
|                        | <b>Number<br/>of<br/>Aircraft</b> | <b>Net Book<br/>Value %</b> | <b>Number<br/>of<br/>Aircraft</b> | <b>Net Book<br/>Value %</b> |
| Europe                 | 56                                | 44%                         | 60                                | 46%                         |
| Asia                   | 32                                | 23%                         | 32 <sup>(1)</sup>                 | 22%                         |
| North America          | 14                                | 12%                         | 14                                | 12%                         |
| Latin America          | 8                                 | 5%                          | 10                                | 8%                          |
| Middle East and Africa | 12                                | 11%                         | 15                                | 12%                         |
| Off-lease              | 8 <sup>(2)</sup>                  | 5%                          |                                   | %                           |
| <b>Total</b>           | <b>130</b>                        | <b>100%</b>                 | <b>131</b>                        | <b>100%</b>                 |

(1) Includes four Boeing Model 737-400 aircraft which will be converted to freighter configuration and for which we have executed leases with a carrier in Asia post-conversion.

(2) Includes one Boeing Model 737-300 aircraft which we delivered on lease to a carrier in the Middle East in the first quarter of 2009, three Boeing Model 737-700 aircraft which we delivered on lease to a carrier in Europe in the first quarter of

2009, two Boeing Model 737-700 aircraft which we delivered on lease to a carrier in Africa in the second quarter of 2009, one Boeing Model 737-700 aircraft which we delivered on lease to a carrier in Latin America in the second quarter of 2009 and one Boeing Model 737-700 aircraft which we delivered on lease to a carrier in Europe in the second quarter of 2009.

At December 31, 2008 and June 30, 2009, lease acquisition costs included in other assets on the consolidated balance sheets were \$293 and \$417, respectively. Prepaid lease incentive costs included in other assets on the consolidated balance sheets were \$5,127 and \$12,708 at December 31, 2008 and June 30, 2009, respectively.

#### Note 4. Securitizations and Term Debt Financings

The outstanding amounts of our securitizations and term debt financing facilities were as follows:

|  | At<br>December 31,<br>2008 |                           | At June 30, 2009                |  |
|--|----------------------------|---------------------------|---------------------------------|--|
|  | Outstanding<br>Borrowings  | Outstanding<br>Borrowings | Interest<br>Rate <sup>(1)</sup> | Final<br>Stated<br>Maturity <sup>(2)</sup> |
| <b>Debt Obligation<br/>Securitizations and Term Debt Financings:</b> |                            |                           |                                 |  |
| Securitization No. 1   | \$ 472,048                 | \$ 461,324                | 0.59%                           | 6/20/31                                    |
| Securitization No. 2   | 1,097,913                  | 1,082,486                 | 0.58%                           | 6/14/37                                    |
| Term Financing No. 1   | 757,610                    | 733,160                   | 2.08%                           | 5/02/15                                    |
| Term Financing No. 2   | 148,725                    | 133,852                   | 3.30%                           | 9/23/13                                    |
| ECA Term Financing   |                            | 70,543                    | 4.48%                           | 5/27/21                                    |
| Total  | \$ 2,476,296               | \$ 2,481,365              |                                 |  |

(1) Reflects floating rate in effect at the applicable

reset date.

- (2) For  
Securitization  
No. 1,  
Securitization  
No. 2 and Term  
Financing No.  
1, all cash flows  
available after  
expenses and  
interest will be  
applied to debt  
amortization, if  
the debt is not  
refinanced by  
June 2011,  
June 2012, and  
May 2013,  
respectively.

In May 2009, we entered into a twelve-year \$70,916 term loan with Citibank International Plc which is supported by a guarantee from Compagnie Francaise d Assurance pour le Commerce Extérieur ( COFACE ), the French government sponsored export credit agency ( ECA ), which we refer to as ECA Term Financing for the financing of a new Airbus Model A330-200 aircraft. The borrowing under the ECA Term Financing bears a fixed rate of interest equal to 4.475%. The obligations outstanding under the ECA Term Financing are secured by, among other things, a mortgage over the aircraft and a pledge of our ownership interest in our subsidiary company that leases the aircraft to

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the operator. The ECA Term Financing documents contain a \$500,000 minimum net worth covenant for Aircastle Limited, as well as a material adverse change default and cross default to any other recourse obligation of Aircastle Limited, and other terms and conditions customary for ECA-supported financings being completed at this time. In addition, Aircastle Limited has guaranteed the repayment of the ECA Term Financing.

The following securitizations and term debt financing structures include liquidity facility commitments described in the table below:

| Facility             | Liquidity Facility Provider | Available Liquidity |                       | Unused Fee | Interest Rate on any Advances   |
|----------------------|-----------------------------|---------------------|-----------------------|------------|---------------------------------|
|                      |                             | December 31, 2008   | June 30, 2009         |            |                                 |
| Securitization No. 1 | Calyon                      | \$42,000            | \$42,000              | 0.45%      | 1M Libor + 1.00%                |
| Securitization No. 2 | HSH Nordbank AG             | 82,343              | 81,186 <sup>(1)</sup> | 0.50%      | 1M Libor + 0.75% <sup>(2)</sup> |
| Term Financing No. 1 | Calyon                      | 15,152              | 14,663                | 0.60%      | 1M Libor + 1.20%                |

(1) Following a ratings downgrade with respect to the liquidity facility provider in May 2009, the liquidity facility was drawn and the proceeds, or permitted investments thereof, remain available to provide liquidity if required.

(2) Amounts drawn following a ratings downgrade with respect to the liquidity facility provider do not bear interest; however, net investment earnings will be paid to the liquidity facility

provider and the  
unused fee  
continues to  
apply.

The purpose of these facilities is to provide liquidity for the relevant securitization or term financing in the event that cash flow from lease contracts and other revenue sources is not sufficient to pay operating expenses with respect to the relevant aircraft portfolio and interest payments and interest rate hedging payments for the relevant securitization or term debt financings. These liquidity facilities are generally 364-day commitments of the liquidity provider and may be extended prior to expiry. If a facility is not extended, or in certain circumstances if the short-term credit rating of the liquidity provider is downgraded, the relevant securitization or term financing documents require that the liquidity facility is drawn and the proceeds of the drawing placed on deposit so that such amounts may be available, if needed, to provide liquidity advances for the relevant securitization or term financing. Downgrade or non-extension drawings are generally not required to be repaid to the liquidity facility provider until 15 days after final maturity of the securitization or term financing debt. In the case of the liquidity facilities for Securitization No. 2 and Term Financing No. 1, the required amount of the facilities reduce over time as the principal balance of the debt amortizes, with the Securitization No. 2 liquidity facility having a minimum required amount of \$65,000.

In May 2009, we were notified of a short-term credit rating downgrade of the liquidity facility provider for Securitization No. 2, HSH Nordbank AG. This downgrade required a drawing of the liquidity facility in cash, which was deposited in a liquidity facility deposit account and held as cash collateral. In June 2009, HSH Nordbank AG directed the investment of this cash into a long-term, AAA-rated investment. We returned the cash in exchange for the long-term investment, which was considered a non-cash transaction and accordingly, at June 30, 2009, an amount of \$81,186 is recorded as an asset on our consolidated balance sheet as Restricted liquidity facility collateral. In addition, the commitment to repay the Securitization No. 2 liquidity facility in the amount of \$81,186 is recorded as a liability on our consolidated balance sheet as Liquidity facility. As of June 30, 2009, the liquidity facilities for Securitization No. 1 and Term Financing No. 1 remain undrawn.

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**Note 5. Dividends**

The table below is a summary of our dividend history for all periods presented. These dividends may not be indicative of the amount of any future dividends.

| <b>Declaration Date</b> | <b>Dividend<br/>per<br/>Common<br/>Share</b> | <b>Aggregate<br/>Dividend<br/>Amount</b> | <b>Record Date</b>    | <b>Payment<br/>Date</b> |
|-------------------------|--|--|-----------------------|-------------------------|
| December 11, 2007       | \$ 0.70                                      | 55,004                                   | December 31,<br>2007  | January 15,<br>2008     |
| March 24, 2008          | \$ 0.25                                      | 19,640                                   | March 31,<br>2008     | April 15,<br>2008       |
| June 11, 2008           | \$ 0.25                                      | 19,647                                   | June 30, 2008         | July 15,<br>2008        |
| September 11, 2008      | \$ 0.25                                      | 19,655                                   | September 30,<br>2008 | October 15,<br>2008     |
| December 22, 2008       | \$ 0.10                                      | 7,862                                    | December 31,<br>2008  | January 15,<br>2009     |
| March 13, 2009          | \$ 0.10                                      | 7,923                                    | March 31,<br>2009     | April 15,<br>2009       |
| June 10, 2009           | \$ 0.10                                      | 7,923                                    | June 30, 2009         | July 15,<br>2009        |

**Note 6. Earnings Per Share**

As described in Note 1 Summary of Significant Accounting Policies, on January 1, 2009 we adopted FSP No. EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities*, which required us to include all common shares granted under our incentive compensation plan which remain unvested ( restricted common shares ) and contain non-forfeitable rights to dividends or dividend equivalents, whether paid or unpaid ( participating securities ), in the number of shares outstanding in our basic and diluted EPS calculations using the two-class method. All of our restricted common shares are currently participating securities.

Under the two-class method, earnings per common share are computed by dividing the sum of distributed earnings allocated to common shareholders and undistributed earnings allocated to common shareholders by the weighted average number of common shares outstanding for the period. In applying the two-class method, distributed and undistributed earnings are allocated to both common shares and restricted common shares based on the total weighted average shares outstanding during the period as follows:

|                                 | <b>Three Months Ended<br/>June 30,</b> |             | <b>Six Months Ended<br/>June 30,</b> |             |
|---------------------------------|--|-------------|--------------------------------------|-------------|
|                                 | <b>2008</b>                            | <b>2009</b> | <b>2008</b>                          | <b>2009</b> |
| <b>Weighted-average shares:</b> |  |             |                                      |             |
| Common shares outstanding       | 77,743,022                             | 77,976,760  | 77,731,504                           | 77,958,980  |
| Restricted common shares        | 896,889                                | 1,389,720   | 871,058                              | 1,287,083   |
| Total weighted-average shares   | 78,639,911                             | 79,366,480  | 78,602,562                           | 79,246,063  |

**Percentage of weighted-average shares:**

|                           |        |        |        |        |
|---------------------------|--------|--------|--------|--------|
| Common shares outstanding | 98.9%  | 98.2%  | 98.9%  | 98.4%  |
| Restricted common shares  | 1.1%   | 1.8%   | 1.1%   | 1.6%   |
| Total                     | 100.0% | 100.0% | 100.0% | 100.0% |



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

|   | <b>Three Months Ended</b> |                | <b>Six Months Ended</b> |                |
|---|---------------------------|----------------|-------------------------|----------------|
|   | <b>June 30,</b>           |                | <b>June 30,</b>         |                |
|   | <b>2008</b>               | <b>2009</b>    | <b>2008</b>             | <b>2009</b>    |
| <b>Earnings per share Basic:</b>  |                           |                |                         |                |
| Net income  | \$ 35,341                 | \$ 27,571      | \$ 66,978               | \$ 46,042      |
| Less: Distributed and undistributed earnings allocated to restricted common shares <sup>(a)</sup> | (403)                     | (483)          | (742)                   | (748)          |
| <br>Earnings available to common shareholders Basic   | <br>\$ 34,938             | <br>\$ 27,088  | <br>\$ 66,236           | <br>\$ 45,294  |
| <br>Weighted-average common shares outstanding Basic  | <br>77,743,022            | <br>77,976,760 | <br>77,731,504          | <br>77,958,980 |
| <br>Earnings per common share Basic   | <br>\$ 0.45               | <br>\$ 0.35    | <br>\$ 0.85             | <br>\$ 0.58    |
| <br><b>Earnings per share Diluted:</b>  |                           |                |                         |                |
| Net income  | \$ 35,341                 | \$ 27,571      | \$ 66,978               | \$ 46,042      |
| Less: Distributed and undistributed earnings allocated to restricted common shares                | (403)                     | (483)          | (742)                   | (748)          |
| <br>Earnings available to common shareholders Diluted   | <br>\$ 34,938             | <br>\$ 27,088  | <br>\$ 66,236           | <br>\$ 45,294  |
| <br>Weighted-average common shares outstanding Basic  | <br>77,743,022            | <br>77,976,760 | <br>77,731,504          | <br>77,958,980 |
| Effect of dilutive shares   | (b)                       | (b)            | (b)                     | (b)            |
| <br>Weighted-average common shares outstanding Diluted  | <br>77,743,022            | <br>77,976,760 | <br>77,731,504          | <br>77,958,980 |
| <br>Earnings per common share Diluted   | <br>\$ 0.45               | <br>\$ 0.35    | <br>\$ 0.85             | <br>\$ 0.58    |

(a)

For the three months ended June 30, 2008 and 2009, distributed and undistributed earnings to restricted shares is 1.1% and 1.8%, respectively, of net income. For the six months ended June 30, 2008 and 2009, distributed and undistributed earnings to restricted shares is 1.1% and 1.6%, respectively, of net income.

- (b) For the three and six months ended June 30, 2008 and 2009, we have no dilutive shares.

#### **Note 7. Income Taxes**

Income taxes have been provided for based upon the tax laws and rates in countries in which our operations are conducted and income is earned. The Company received an assurance from the Bermuda Minister of Finance that it would be exempted from local income, withholding and capital gains taxes until March 2016. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily the United States and Ireland.

The sources of income from continuing operations before income taxes for the three and six months ended June 30, 2008 and 2009 were as follows:

|                     | <b>Three Months Ended<br/>June 30,</b> |             | <b>Six Months Ended<br/>June 30,</b> |             |
|---------------------|--|-------------|--------------------------------------|-------------|
|                     | <b>2008</b>                            | <b>2009</b> | <b>2008</b>                          | <b>2009</b> |
| U.S. operations     | \$ 353                                 | \$ 502      | \$ 988                               | \$ 959      |
| Non-U.S. operations | 36,621                                 | 29,118      | 69,337                               | 49,048      |
| Total               | \$ 36,974                              | \$ 29,620   | \$ 70,325                            | \$ 50,007   |

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All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. We also have a U.S.-based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes.

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

|  | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |             |
|--|---------------------------|-------------|-------------------------|-------------|
|  | <b>June 30,</b>           |             | <b>June 30,</b>         |             |
|  | <b>2008</b>               | <b>2009</b> | <b>2008</b>             | <b>2009</b> |
| Notional U.S. federal income tax expense at the statutory rate | \$ 12,942                 | \$ 10,367   | \$ 24,614               | \$ 17,502   |
| U.S. state and local income tax, net                           | 51                        | 26          | 78                      | 49          |
| Non-U.S. operations  | (11,377)                  | (8,638)     | (21,361)                | (13,906)    |
| Non-deductible expenses in the U.S.                            | 13                        | 7           | 21                      | 15          |
| Other  | 4                         | 287         | (5)                     | 305         |
| Provision for income taxes                                     | \$ 1,633                  | \$ 2,049    | \$ 3,347                | \$ 3,965    |

**Note 8. Comprehensive Income (Loss)**

Total comprehensive income (loss) includes net income, the changes in the fair value and the reclassification into earnings of amounts previously deferred relating to our derivative financial instruments which qualify for hedge accounting in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, and the change in unrealized fair value of debt securities classified as available-for-sale. Total comprehensive income (loss) for the three and six months ended June 30, 2008 and 2009 was as follows:

|   | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |             |
|---|---------------------------|-------------|-------------------------|-------------|
|   | <b>June 30,</b>           |             | <b>June 30,</b>         |             |
|   | <b>2008</b>               | <b>2009</b> | <b>2008</b>             | <b>2009</b> |
| Net income  | \$ 35,341                 | \$ 27,571   | \$ 66,978               | \$ 46,042   |
| Net change in fair value of derivatives, net of tax expense of \$1,453 and \$972 for the three months ended and \$189 and \$1,203 for the six months ended June 30, 2008 and 2009, respectively | 103,090                   | 37,554      | (29,690)                | 27,357      |
| Derivative loss reclassified into earnings  | 15,016                    | 30,613      | 24,286                  | 59,731      |
| Net change in unrealized fair value of debt investments   | (1,595)                   | 936         | (2,014)                 | (138)       |
| Total comprehensive income (loss)   | \$ 151,852                | \$ 96,674   | \$ 59,560               | \$ 132,992  |

The following table sets forth the components of accumulated other comprehensive income (loss), net of tax where applicable, at December 31, 2008 and June 30, 2009:

**Accumulated  
Other**

|   | <b>Fair Value<br/>of<br/>Derivatives</b> | <b>Fair Value<br/>of<br/>Debt<br/>Securities</b> | <b>Comprehensive<br/>Income (Loss)</b> |
|---|--|--|--|
| December 31, 2008   | \$ (365,138) <sup>(1)</sup>              | \$ 2,536   | \$ (362,602)                           |
| Net change in fair value of derivatives, net of tax expense<br>of \$1,203 | 27,357                                   |  | 27,357                                 |
| Derivative loss reclassified into earnings                                | 59,731                                   |  | 59,731                                 |
| Net change in unrealized fair value of debt investments                   |  | (138)  | (138)                                  |
| June 30, 2009   | \$ (278,050)                             | \$ 2,398   | \$ (275,652)                           |

(1) Net of tax benefit of \$4,530 at December 31, 2008.

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**Note 9. Commitments and Contingencies**

We have an acquisition agreement, which we refer to as the Airbus A330 Agreement, with Airbus S.A.S, or Airbus, under which we agreed to acquire from Airbus twelve new A330-200 aircraft, or the New A330 Aircraft. In February 2009, we amended the Airbus A330 Agreement to defer the scheduled delivery of an aircraft from the fourth quarter of 2010 to the first half of 2012. On May 27, 2009, we advanced one of the New A330 Aircraft positions and took delivery of an Airbus Model A330-200 aircraft and placed it on lease with a customer. In July 2009, we amended the Airbus A330 Agreement to defer the scheduled delivery of an aircraft from 2010 to 2011.

As of June 30, 2009, we had paid \$89,244 in Airbus deposits and pre-delivery payments, in relation to the 11 New A330 Aircraft remaining to be delivered under the Airbus A330 Agreement, and recorded \$5,041 in capitalized interest. Under certain circumstances, we have the right to change the delivery positions to alternative A330 aircraft models. Three of the New A330 Aircraft are scheduled to be delivered in 2010, five are scheduled to be delivered in 2011 and the remaining three are scheduled to be delivered in 2012.

As a result of the July 2009 amendment to the Airbus A330 Agreement, our committed amounts to acquire, convert and modify aircraft including, where applicable, our estimate of adjustments for configuration changes, engine acquisition costs, contractual price escalations and other adjustments, net of amounts already paid, are approximately \$47,880 in 2009, \$236,939 in 2010, \$377,778 in 2011 and \$156,322 in 2012.

**Note 10. Derivatives**

As described in Note 1 – Summary of Significant Accounting Policies, the Company adopted SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* on January 1, 2009. SFAS No. 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows.

In the normal course of business we utilize interest rate derivatives to manage our exposure to interest rate risks. Specifically, our interest rate derivatives are hedging variable rate interest payments on our various debt facilities. We account for our interest rate derivatives in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended and interpreted, or SFAS No. 133. Under SFAS No. 133, if certain conditions are met, an interest rate derivative may be specifically designated as a cash flow hedge. All of our designated interest rate derivatives are cash flow hedges. We have one interest rate derivative that is not designated under SFAS No. 133.

On the date that we enter into an interest rate derivative, we formally document the intended use of the interest rate derivative and its designation as a cash flow hedge, if applicable. We also assess (both at inception and on an ongoing basis) whether the interest rate derivative has been highly effective in offsetting changes in the cash flows of the variable rate interest payments on our debt and whether the interest rate derivative is expected to remain highly effective in future periods. If it were to be determined that the interest rate derivative is not (or has ceased to be) highly effective as a cash flow hedge, we would discontinue SFAS No. 133 accounting prospectively.

At inception of an interest rate derivative designated as a cash flow hedge, we establish the method we will use to assess effectiveness and the method we will use to measure any ineffectiveness. Historically, we have elected to use the change in variable cash flows method for both. This method involves a comparison of the present value of the cumulative change in the expected future cash flows on the variable leg of the interest rate derivative against the present value of the cumulative change in the expected future interest cash flows on the variable-rate debt. When the change in the interest rate derivative's variable leg exceeds the change in the debt's variable-rate interest cash flows, the calculated ineffectiveness is recorded in interest expense on our consolidated statement of income. Effectiveness is assessed by dividing the change in the interest rate derivative variable leg by the change in the debt's variable-rate interest cash flows.

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We use the hypothetical trade method for interest rate derivatives designated as cash flow hedges subsequent to inception that did not qualify for the change in variable cash flow method under SFAS No. 133. The calculation involves a comparison of the change in the fair value of the interest rate derivative to the change in the fair value of a hypothetical interest rate derivative with critical terms that reflect the hedged variable-rate debt. The effectiveness of these relationships is assessed by regressing historical changes in the interest rate derivative against historical changes in the hypothetical interest rate derivative. When the change in the interest rate derivative exceeds the change in the hypothetical interest rate derivative, the calculated ineffectiveness is recorded in interest expense on our consolidated statement of income.

In accordance with SFAS No. 133 and SFAS No. 157, all interest rate derivatives are recognized on the balance sheet at their fair value. We determine fair value for our United States dollar denominated interest rate derivatives by calculating reset rates and discounting cash flows based on cash rates, futures rates and swap rates in effect at the period close. We determine the fair value of our United States dollar denominated guaranteed notional balance interest rate derivatives based on the upper notional band using cash flows discounted at relevant market interest rates in effect at the period close. See Note 2 Fair Value Measurements for more information.

For our interest rate derivatives designated as cash flow hedges under SFAS No. 133, the effective portion of the interest rate derivative's gain or loss is initially reported as a component of other comprehensive income and subsequently reclassified into earnings when the interest payments on the debt are recorded in earnings. The ineffective portion of the interest rate derivative is calculated and recorded in interest expense on our consolidated statement of income at each quarter end. For any interest rate derivative not designated as a cash flow hedge under SFAS No. 133, the gain or loss is recognized in other income (expense) on our consolidated statement of income.

We may choose to terminate certain interest rate derivatives prior to their contracted maturities. Any related net gains or losses in accumulated other comprehensive income at the date of termination are not reclassified into earnings if it remains probable that the interest payments on the debt will occur. The amounts in accumulated other comprehensive income are reclassified into earnings as the interest payments on the debt affect earnings. Terminated interest rate derivatives are reviewed periodically to determine if the forecasted transactions remain probable of occurring. To the extent that the occurrence of the interest payments on the debt are deemed remote, the related portion of the accumulated other comprehensive income balance is reclassified into earnings immediately.

Our interest rate derivatives involve counterparty credit risk. As of June 30, 2009, our interest rate derivatives are held with the following counterparties: JP Morgan Chase Bank NA, Citibank Canada NA, HSH Nordbank AG and DVB Bank SE. All of our counterparties or guarantors of these counterparties are considered investment grade (senior unsecured ratings of A3 or above by Moody's Investors Service and long-term foreign issuer ratings of BBB+ or above by Standard and Poor's). As a result, we do not anticipate that any of these counterparties will fail to meet their obligations.

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**June 30, 2009**

We held the following interest rate derivatives as of June 30, 2009:

|  | <b>Liability Derivatives</b>   |                       |                      |                                       |                      |                   |                                      | <b>Fair Value</b> |
|--|--------------------------------|-----------------------|----------------------|---------------------------------------|----------------------|-------------------|--------------------------------------|-------------------|
|  | <b>Current Notional Amount</b> | <b>Effective Date</b> | <b>Maturity Date</b> | <b>Future Maximum Notional Amount</b> | <b>Floating Rate</b> | <b>Fixed Rate</b> | <b>Balance Sheet Location</b>        |                   |
| <b>Hedged Item</b>   | <b>Amount</b>                  | <b>Date</b>           | <b>Date</b>          | <b>Amount</b>                         | <b>Rate</b>          | <b>Rate</b>       | <b>Location</b>                      |                   |
| <b>Interest rate derivatives designated as cash flow hedges under Statement 133:</b>     |                                |                       |                      |                                       |                      |                   |                                      |                   |
| Securitization No. 1   | \$ 461,324                     | Jun-06                | Jun-16               | \$ 461,324                            | 1M LIBOR + 0.27%     | 5.78%             | Fair value of derivative liabilities | \$ 54,121         |
| Securitization No. 2   | 1,073,895                      | Jun-07                | Jun-12               | 1,073,895                             | 1M LIBOR             | 5.25% to 5.36%    | Fair value of derivative liabilities | 95,328            |
| Term Financing No. 1 <sup>(1)</sup>  | 665,658                        | Jun-08                | May-13               | 665,658                               | 1M LIBOR             | 4.04%             | Fair value of derivative liabilities | 34,664            |
| Term Financing No. 1 <sup>(1)</sup>  |                                | May-13                | May-15               | 491,718                               | 1M LIBOR             | 5.31%             | Fair value of derivative liabilities | 4,176             |
| Total interest rate derivatives designated as cash flow hedges under Statement 133       | 2,200,877                      |                       |                      | 2,692,595                             |                      |                   |                                      | 188,289           |
| <b>Interest rate derivatives not designated as cash flow hedges under Statement 133:</b> |                                |                       |                      |                                       |                      |                   |                                      |                   |
| Term Financing No. 2 <sup>(2)</sup>  | 119,870                        | Oct-08                | Sep-13               | 119,870                               | 3M LIBOR             | 3.17%             | Fair value of derivative liabilities | 3,122             |

|  |              |              |            |
|--|--------------|--------------|------------|
| Total interest rate derivatives not designated as cash flow hedges under Statement 133 | 119,870      | 119,870      | 3,122      |
| Total interest rate derivatives  | \$ 2,320,747 | \$ 2,812,465 | \$ 191,411 |

(1) The interest payments related to Term Financing No. 1 are being hedged by two consecutive interest rate derivatives. When the first matures in May 2013, the next becomes effective.

(2) Although we entered into this interest rate derivative to hedge the variable rate interest payments in connection with Term Financing No. 2, it has not been designated as a hedge for accounting purposes.

In addition to the derivative liability above, another component of the fair value of our interest rate derivatives is accrued interest. As of June 30, 2009, accrued interest payable included in accounts payable, accrued expenses, and other liabilities on our consolidated balance sheet was \$5,896 related to interest rate derivatives designated as cash flow hedges and \$68 for interest rate derivatives not designated as cash flow hedges.

The amount of loss expected to be reclassified from accumulated OCI into interest expense over the next 12 months consists of net interest settlements on active interest rate derivatives disclosed above, in the amount of \$91,911 and the amortization of deferred net losses in the amount of \$7,900. For the six months ended June 30, 2009, the amount of loss reclassified from accumulated OCI into interest expense consisted of net interest settlements on active interest rate derivatives in the amount of \$49,177, and the amortization of deferred net losses in the amount of



\$4,092 as disclosed below.

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Following is the effect of interest rate derivatives on the statement of financial performance for the six months ended June 30, 2009:

| <b>Derivatives in</b>     | <b>Effective Portion</b>  |  | <b>Amount of</b><br><b>Gain or (Loss)</b><br><b>Reclassified</b><br><b>from</b><br><b>Accumulated</b><br><b>OCI into Income</b> | <b>Ineffective Portion</b>   |   |
|---------------------------|---|--|---|--|---|
|                           | <b>Amount of</b><br><b>Gain or (Loss)</b><br><b>Recognized in</b><br><b>OCI on</b><br><b>Derivative</b><br><b>(a)</b> | <b>Location of</b><br><b>Gain or (Loss)</b><br><b>Reclassified</b><br><b>from</b><br><b>Accumulated</b><br><b>OCI into</b><br><b>Income</b><br><b>Interest</b><br><b>expense</b> |   | <b>Amount of</b><br><b>Gain or (Loss)</b><br><b>Recognized in</b><br><b>Income on</b><br><b>Derivative</b><br><b>(c)</b> | <b>Location</b><br><b>of</b><br><b>Gain or</b><br><b>(Loss)</b><br><b>Recognized</b><br><b>in</b><br><b>Income on</b><br><b>Derivative</b><br><b>Interest</b><br><b>expense</b> |
| <b>Statement 133</b>      |   |  |   |  |   |
| <b>Cash Flow</b>          |   |  |   |  |   |
| <b>Hedging</b>            |   |  |   |  |   |
| <b>Relationships</b>      |   |  |   |  |   |
| Interest rate derivatives | \$27,357  | Interest expense   | \$(53,269)  | Interest expense   | \$2,690 <sup>(1)</sup>  |

(a) This represents the change in fair market value of our interest rate derivatives since year end, net of taxes, offset by the amount of actual cash paid related to the net settlements of the interest rate derivatives for each month of the six months ended June 30, 2009.

(b) This represents the amount of actual cash paid related to the net settlements of the interest rate derivatives for each month of the six months

ended June 30, 2009 plus any effective amortization of net deferred interest rate derivative losses.

(c) This represents both realized and unrealized ineffectiveness incurred during the six months ended June 30, 2009.

(1) Excludes losses of \$3,704 and \$2,758 which were charged to interest expense during the six months ended June 30, 2009 as a result of changes in projected future debt related to the New A330 Aircraft and partial termination of a Securitization No. 1 interest rate derivative, respectively. See the table below, which summarizes amounts charged to the consolidated statement of income related to our interest rate derivatives.

**Derivatives Not Designated as**

**Location of Gain or (Loss)**

**Amount of Gain or (Loss)**

**Hedging Instruments  
under Statement 133**

**Recognized in Income  
On Derivative**

**Recognized in Income  
on Derivative**

Interest rate derivatives

Other income (expense)

\$1,164

Generally, our interest rate derivatives are hedging current interest payments on debt and future interest payments on long-term debt. In the past, we have entered into forward-starting interest rate derivatives to hedge the anticipated interest payment on long-term financings. These interest rate derivatives were terminated and new, specifically tailored interest rate derivatives were entered into upon closing of the relevant long-term financing. We have also early terminated interest rate derivatives in an attempt to manage our exposure to collateral calls. We have no active interest rate derivatives in effect in relation to the anticipated interest payments on long-term financings required for our New A330 Aircraft.

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The following table summarizes the deferred (gains) and losses for our terminated interest rate derivatives and the related amortization into interest expense for the six months ended June 30, 2008 and 2009:

| Hedged Item                        | Original<br>Maximum<br>Notional<br>Amount | Effective<br>Date | Fixed<br>Rate<br>% | Termination<br>Date | Deferred<br>Gain<br>or<br>Loss<br>upon<br>Termination | Unamortized<br>Deferred<br>(Gain)<br>or<br>Loss at<br>June<br>30,<br>2009 | Amount of<br>Deferred<br>(Gain) or Loss<br>Amortized<br>(including<br>Accelerated<br>Amortization)<br>into<br>Interest Expense<br>for |            | Amount<br>of<br>Deferred<br>(Gain)<br>or<br>Loss<br>expected<br>to<br>be<br>amortized<br>over<br>the<br>next<br>twelve<br>months |
|------------------------------------|---|-------------------|--------------------|---------------------|---|---|---|------------|--|
|                                    |   |                   |                    |                     |   |   | the Six Months<br>Ended June 30,<br>2008  | 2009       |  |
| Securitization No. 1               | \$ 400,000                                | Dec-05            | 104.61             | Jun-06              | \$ (13,397)   | \$ (3,363)  | \$ (1,630)  | \$ (1,557) | \$ (2,999)   |
| Securitization No. 1               | 200,000                                   | Dec-05            | 105.03             | Jun-06              | (2,541)   | (542)   | (288)   | (185)      | (327)  |
|                                    |   |                   |                    | Partial             |   |   |   |            |  |
| Securitization No. 1               | 451,911                                   | Jun-06            | 165.78             | Apr-09              | 2,758   |   |   | 2,758      |  |
| Securitization No. 2               | 500,000                                   | Mar-06            | 115.07             | Jun-07              | (2,687)   | (1,151)   | (377)   | (359)      | (697)  |
| Securitization No. 2               | 200,000                                   | Jan-07            | 125.06             | Jun-07              | (1,850)   | (1,056)   | (195)   | (185)      | (360)  |
| Securitization No. 2               | 410,000                                   | Feb-07            | 175.14             | Jun-07              | (3,119)   | (2,206)   | (232)   | (202)      | (380)  |
| Term Financing No. 1               | 150,000                                   | Jul-07            | 175.14             | Mar-08              | 15,281  | 12,411  | 666   | 1,045      | 1,986  |
|                                    |   |                   |                    | Partial             |   |   |   |            |  |
| Term Financing No. 1               | 440,000                                   | Jun-07            | 134.88             | Mar-08              | 26,281  | 18,872  | 1,219   | 3,045      | 5,788  |
|                                    |   |                   |                    | Full<br>Jun-08      |   |   |   |            |  |
| Term Financing No. 1               | 248,000                                   | Aug-07            | 135.33             | Jun-08              | 9,888   | 7,459   | 132   | 1,130      | 2,148  |
| Term Financing No. 2               | 55,000                                    | May-08            | 145.41             | Jun-08              | 2,380   |   | 6   |            |  |
|                                    |   |                   |                    | Partial             |   |   |   |            |  |
| Term Financing No. 2               | 360,000                                   | Jan-08            | 195.16             | Jun-08              | 23,077  | 13,217  | 167   | 1,361      | 2,300  |
|                                    |   |                   |                    | Full<br>Oct-08      |   |   |   |            |  |
| Repurchase Agreement               | 74,000                                    | Feb-06            | 105.02             | Feb-08              | 878   |   | 878   |            |  |
| Repurchase Agreement               | 5,000                                     | Dec-05            | 094.94             | Mar-08              | 144   |   | 144   |            |  |
| Repurchase Agreement               | 2,900                                     | Jun-05            | 134.21             | Jun-08              | (19)  |   | (19)  |            |  |
| ECA Term Financing and future debt | 238,000                                   | Jan-07            | 165.23             | Dec-08              | 19,430  | 18,490  |   | 940        |  |
| Future debt and securitization     | 231,000                                   | Apr-06            | 155.17             |                     | 15,310  | 13,053  |   | 674        |  |

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|                                |         | Partial<br>Jun-08 | Full<br>Dec-08 |                      |           |        |           |          |
|--------------------------------|---------|-------------------|----------------|----------------------|-----------|--------|-----------|----------|
| Future debt and securitization | 203,000 | Jun-07-124.89     | Dec-08         | 2,728 <sup>(1)</sup> | 496       | 59     | 968       | 441      |
| Future debt and securitization | 238,000 | Jul-Sep-165.27    | Dec-08         | 17,254               | 16,133    |        | 1,121     |          |
| Total                          |         |                   |                | \$ 111,796           | \$ 91,813 | \$ 530 | \$ 10,554 | \$ 7,900 |

(1) The deferred loss for this interest rate derivative is related to the period prior to de-designation.

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**June 30, 2009**

The following table summarizes amounts charged directly to the consolidated statement of income for the three and six months ended June 30, 2008 and 2009, respectively, related to our interest rate derivatives:

|   | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |             |
|---|---------------------------|-------------|-------------------------|-------------|
|   | <b>June 30,</b>           |             | <b>June 30,</b>         |             |
|   | <b>2008</b>               | <b>2009</b> | <b>2008</b>             | <b>2009</b> |
| <b>Interest Expense:</b>  |                           |             |                         |             |
| Hedge ineffectiveness (gains) losses (unrealized)                       | \$ 3,907                  | \$ (3,202)  | \$ 5,905                | \$ (3,331)  |
| Amortization:   |                           |             |                         |             |
| Accelerated amortization of deferred losses                             | 122                       | 829         | 122                     | 3,704       |
| Amortization of deferred (gains) losses                                 | 565                       | 2,018       | (595)                   | 4,092       |
| (Gains) Losses on termination of interest rate derivatives              | (18)                      | 2,758       | 1,003                   | 2,758       |
| Total Amortization  | 669                       | 5,605       | 530                     | 10,554      |
| Total charged to interest expense                                       | \$ 4,576                  | \$ 2,403    | \$ 6,435                | \$ 7,223    |
| <b>Other Income:</b>  |                           |             |                         |             |
| Mark to market gains (losses) on undesignated interest rate derivatives | \$ 731                    | \$ 1,072    | \$ 731                  | \$ 1,164    |
| Total charged to other income   | \$ 731                    | \$ 1,072    | \$ 731                  | \$ 1,164    |

The weighted average interest pay rates of these derivatives were 4.90% at both December 31, 2008 and June 30, 2009.

As of June 30, 2009, we did not have any cash collateral pledged under our interest rate derivatives, nor do we have any existing agreements that require cash collateral postings.

**Note 11. Interest, Net**

The following table shows the components of interest, net:

|  | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |             |
|--|---------------------------|-------------|-------------------------|-------------|
|  | <b>June 30,</b>           |             | <b>June 30,</b>         |             |
|  | <b>2008</b>               | <b>2009</b> | <b>2008</b>             | <b>2009</b> |
| Interest on borrowings and other liabilities                                 | \$ 46,171                 | \$ 36,642   | \$ 88,050               | \$ 73,412   |
| Hedge ineffectiveness (gains) losses (unrealized)                            | 3,907                     | (3,202)     | 5,905                   | (3,331)     |
| Amortization of interest rate derivatives related to deferred (gains) losses | 687                       | 2,847       | (473)                   | 7,796       |
| (Gains) losses on termination of interest rate derivatives                   | (18)                      | 2,758       | 1,003                   | 2,758       |
| Amortization of deferred financing fees                                      | 4,203                     | 3,198       | 6,787                   | 5,731       |
| Interest Expense   | 54,950                    | 42,243      | 101,272                 | 86,366      |
| Less interest income   | (2,827)                   | (416)       | (4,558)                 | (857)       |
| Less capitalized interest  | (804)                     | (345)       | (4,384)                 | (616)       |

|               |           |           |           |           |
|---------------|-----------|-----------|-----------|-----------|
| Interest, net | \$ 51,319 | \$ 41,482 | \$ 92,330 | \$ 84,893 |
|---------------|-----------|-----------|-----------|-----------|

**Note 12. Shareholders Equity and Share Based Payment**

In January 2009, the Company granted restricted common shares to employees with a total fair value of \$2,846. The 597,350 restricted common shares granted had grant prices which ranged between \$4.42 and \$5.36 per share. Of these restricted common shares, 347,350 vest over three years. The remaining 250,000 restricted common shares vest over five years. In February 2009, the Company granted 125,000 restricted common shares to certain directors with a total fair value of \$351. The shares vest on January 1, 2010. The fair value of the restricted common shares granted is determined based upon the market price of the common shares at grant date.



**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

This management's discussion and analysis of financial condition and results of operations contains forward-looking statements that involve risks, uncertainties and assumptions. You should read the following discussion in conjunction with our historical consolidated financial statements and the notes thereto appearing elsewhere in this report. The results of operations for the periods reflected herein are not necessarily indicative of results that may be expected for future periods, and our actual results may differ materially from those discussed in the forward-looking statements as a result of various factors, including but not limited to those described under Risk Factors and included in our Annual Report on Form 10-K for the year ended December 31, 2008 filed with the Securities and Exchange Commission (the SEC). Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States, or GAAP. All references to dollars and \$ in this report are to, and all monetary amounts in this report are presented in, U.S. dollars.

Certain items in this Quarterly Report on Form 10-Q (this report), and other information we provide from time to time, may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 including, but not necessarily limited to, statements relating to our ability to acquire, sell and lease aircraft, raise capital, pay dividends, and increase revenues, earnings and EBITDA and the global aviation industry and aircraft leasing sector. Words such as anticipates, expects, intends, plans, projects, believes, may, will, would, seeks, estimates and variations on these words and similar expressions are intended to identify such forward-looking statements. These statements are based on management's current expectations and beliefs and are subject to a number of factors that could lead to actual results materially different from those described in the forward-looking statements; Aircastle Limited can give no assurance that its expectations will be attained. Accordingly, you should not place undue reliance on any forward-looking statements contained in this report. Factors that could have a material adverse effect on our operations and future prospects or that could cause actual results to differ materially from Aircastle Limited's expectations include, but are not limited to, prolonged capital markets disruption and volatility, which may adversely affect our continued ability to obtain additional capital to finance our working capital needs, our pre-delivery payment obligations and other aircraft acquisition commitments, our ability to extend or replace our existing financings, and the demand for and value of aircraft; our exposure to increased bank and counterparty risk caused by credit and capital markets disruptions; general economic conditions and business conditions affecting demand for aircraft and lease rates; our continued ability to obtain favorable tax treatment in Bermuda, Ireland and other jurisdictions; our ability to pay dividends; high or volatile fuel prices, lack of access to capital, reduced load factors and yields and other factors affecting the creditworthiness of our airline customers and their ability to continue to perform their obligations under our leases; termination payments on our interest rate hedges; and other risks detailed from time to time in Aircastle Limited's filings with the SEC, including Risk Factors as previously disclosed in Aircastle's 2008 Annual Report on Form 10-K, and elsewhere in this report. In addition, new risks and uncertainties emerge from time to time, and it is not possible for Aircastle to predict or assess the impact of every factor that may cause its actual results to differ from those contained in any forward-looking statements. Such forward-looking statements speak only as of the date of this report. Aircastle Limited expressly disclaims any obligation to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in its expectations with regard thereto or change in events, conditions or circumstances on which any statement is based.

**WEBSITE AND ACCESS TO COMPANY'S REPORTS**

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

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

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**OVERVIEW**

We are a global company that acquires, leases, and sells high-utility commercial jet aircraft to passenger and cargo airlines throughout the world. High-utility aircraft are generally modern, operationally efficient jets with a large operator base and long useful lives. As of June 30, 2009, our aircraft portfolio consisted of 131 aircraft and we had 60 lessees located in 35 countries. At June 30, 2009, the average age of the aircraft in our portfolio was 10.7 years and the average remaining lease term was 5.0 years, in each case weighted by net book value. Our revenues and income from continuing operations for the three and six months ended June 30, 2009 were \$136.9 million and \$29.6 million and \$269.1 million and \$50.0 million, respectively.

Although current market conditions have significantly reduced the availability of equity and debt capital, we plan to grow our business and profits over the long term by continuing to employ our fundamental business strategy which includes:

- (1) Selectively investing in additional commercial jet aircraft and other aviation assets when attractively priced opportunities and cost effective financing are available;
- (2) Maintaining an efficient capital structure by using varying long-term debt structures to obtain cost effective financing and leveraging the efficient operating platform we have established; and
- (3) Reinvesting a portion of the cash flows generated by our business and from selective asset dispositions in additional aviation assets and/or our own debt and equity securities.

We believe our team's capabilities in the global aircraft leasing market place us in a favorable position to explore new income-generating activities when capital becomes available for such activities. However, the financial markets continue to be under considerable distress. It is not clear when credit will become readily available in sufficient volume to satisfy the financing and refinancing needs in the aviation industry. If current levels of financial market disruption continue or worsen, there can be no assurance that we will not experience an adverse effect, which may be material, on our ability to access capital, on our cost of capital or on our business, financial condition or results of operations.

In addition to the current financial markets turmoil, the global economic slowdown has reduced both passenger and cargo air traffic, as evidenced by the sharp drop in traffic levels during the past few months. The International Air Transport Association reported year on year declines in international passenger traffic for the first six months in 2009 of more than 8% and declines in international freight traffic in excess of 20%. This has translated into increased financial pressures on airlines as well as reduced demand for aircraft. With an average remaining lease term of 5.0 years and relatively modest scheduled releasing requirements over the next year, we believe our portfolio is well positioned. Our management team has significant experience in the leasing and technical management of aviation assets, and extensive experience managing lease restructuring and aircraft repossessions, which we believe is critical to mitigate our customer default exposure. However, we expect the business environment will continue to be very challenging for the aircraft leasing industry throughout 2009 and perhaps beyond.

We intend to pay regular quarterly dividends to our shareholders. On March 13, 2009, our board of directors declared a first quarter dividend of \$0.10 per common share, or an aggregate of \$7.9 million, for the three months ended March 31, 2009, which was paid on April 15, 2009 to holders of record on March 31, 2009. On June 10, 2009, our board of directors declared a second quarter dividend of \$0.10 per common share, or an aggregate of \$7.9 million, for the three months ended June 30, 2009, which was paid on July 15, 2009 to shareholders of record on June 30, 2009. These dividends may not be indicative of the amount of any future dividends.

**Revenues**

Our revenues are comprised primarily of operating lease rentals on flight equipment held for lease. In addition, we recognize revenue from retained maintenance payments related to lease expirations. We also earn interest income from our debt investments.

Typically, our aircraft are subject to net operating leases whereby the lessee pays lease rentals and is generally responsible for maintaining the aircraft and paying operational, maintenance and insurance costs, although in a majority of cases we are obligated to pay a portion of specified maintenance or modification costs. Our aircraft lease

agreements

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generally provide for the periodic payment of a fixed amount of rent over the life of the lease and the amount of the contracted rent will depend upon the type, age, specification and condition of the aircraft, and market conditions at the time the lease is committed. The amount of rent we receive will depend on a number of factors, including the credit-worthiness of our lessees and the occurrence of delinquencies, restructurings and defaults. Our lease rental revenues are also affected by the extent to which aircraft are off-lease and our ability to remarket aircraft that are nearing the end of their leases in order to minimize their off-lease time. Our success in re-leasing aircraft is affected by market conditions relating to our aircraft and by general industry conditions and trends. An increase in the percentage of off-lease aircraft or a reduction in lease rates upon remarketing would negatively impact our revenues.

**2009 Lease Expirations and Lease Placements**

*Scheduled lease expirations placements.* For our 20 owned aircraft originally having lease expirations in 2009, we executed leases and lease renewals, or commitments to lease or renew, with respect to 19 aircraft, including one aircraft we have taken back earlier than originally scheduled in 2009 on a consensual basis from a lessee. We are actively marketing the remaining aircraft. We estimate that, for the 20 aircraft, the weighted average lease term for the new leases or renewals will be approximately six years with monthly lease rates that are approximately six percent higher than the previous rentals.

*Aircraft acquisitions placements.* In May 2009, we took delivery of one new A330-200 aircraft and immediately placed it on lease with Aerovias del Continente Americano, or Avianca, a new customer. We currently have no commitment to acquire additional aircraft in 2009.

*Repossessions and other lease transitions placements.* In 2009, we delivered on lease eight aircraft we repossessed in 2008. In addition to the early transition mentioned in Scheduled lease expiration placements above, we completed a consensual early lease termination for four aircraft in 2009:

Two Airbus Model A320-200 aircraft, which were placed on lease with new customers in the first and second quarters, respectively, of 2009.

One Boeing Model 767-300ER aircraft, for which we have an executed short-term lease with a scheduled delivery in August 2009, and which we are currently marketing for lease starting in the first quarter of 2010.

One Boeing Model 737-300 aircraft, which was returned to us in the third quarter of 2009 and for which we have a non-binding letter of intent for sale.

We have also agreed to an early termination of one Airbus Model A330-300 aircraft with an originally scheduled lease expiry in 2011 and have a commitment to lease this aircraft to another customer upon return, which is expected to occur in the fourth quarter of 2009.

**2010 Lease Expirations and Lease Placements**

*Scheduled lease expirations placements.* For our 19 owned aircraft originally having lease expirations in 2010, we have executed lease renewals, or commitments to lease or renew, with respect to seven aircraft, we have signed sale agreements to sell two aircraft and we are actively remarketing the remaining ten aircraft. As mentioned above, one Boeing Model 767-300ER is expected to deliver on a short-term lease in 2009 and we are also actively marketing this aircraft for lease in the first quarter of 2010.

*Aircraft acquisitions placements.* In February 2009, we amended the Airbus A330 Agreement to defer the scheduled delivery of an aircraft from the fourth quarter of 2010 to the first half of 2012 and in July 2009 we amended the Airbus A330 Agreement to defer the scheduled delivery of an aircraft from 2010 to 2011. We are scheduled to take delivery of two of the new A330-200 Aircraft, both in the second half of 2010. We have executed lease agreements for both aircraft with a carrier in Asia. We currently have no other commitment to acquire aircraft in 2010.



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**2011-2014 Lease Expirations and Lease Placements**

*Scheduled lease expirations placements.* We have 11 owned aircraft originally having lease expirations scheduled in 2011. We have executed lease renewals, or commitments to lease or renew, with respect to three of these aircraft, and we have a signed sale agreement to sell one aircraft. We are actively remarketing the remaining seven aircraft. We currently have 69 aircraft with lease expirations scheduled in the period 2012-2014.

*Aircraft acquisitions placements.* We are scheduled to take delivery of six of the New A330 Aircraft in 2011 and three in 2012, and we are actively remarketing the remaining aircraft. We have executed a lease agreement for one of the New A330 Aircraft scheduled for delivery in 2011 with a carrier in Asia. We currently have no other commitment to acquire aircraft in the period 2011-2014.

**Operating Expenses**

Operating expenses are comprised of depreciation of flight equipment held for lease, interest expense, selling, general and administrative expenses, or SG&A, and maintenance and other costs. Because our operating lease terms generally require the lessee to pay for operating, maintenance and insurance costs, our portion of maintenance and other costs relating to aircraft reflected in our statement of income has been nominal; however, to the extent our customers fail to pay operating, maintenance, insurance or transition costs, our portion of these expenses reflected in our income statement would increase.

**Income Tax Provision**

We have obtained an assurance from the Minister of Finance of Bermuda under the Exempted Undertakings Tax Protection Act 1966 that, in the event that any legislation is enacted in Bermuda imposing any tax computed on profits or income, or computed on any capital asset, gain or appreciation or any tax in the nature of estate duty or inheritance tax, such tax shall not, until March 28, 2016, be applicable to us or to any of our operations or to our shares, debentures or other obligations except insofar as such tax applies to persons ordinarily resident in Bermuda or to any taxes payable by us in respect of real property owned or leased by us in Bermuda. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily Ireland and the United States.

All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. We also have a U.S.-based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes.

**Acquisitions and Dispositions**

We have an acquisition agreement, or the Airbus A330 Agreement, with Airbus S.A.S, or Airbus, under which we agreed to acquire from Airbus twelve new A330-200 aircraft, or the New A330 Aircraft. In February 2009, we amended the Airbus A330 Agreement to defer the scheduled delivery of an aircraft from the fourth quarter of 2010 to the first half of 2012. On May 27, 2009, we advanced one of the New A330 Aircraft positions and took delivery of one A330-200 aircraft and placed it on lease with Avianca, a new customer. In July 2009 we agreed with Airbus to defer one of the 2010 delivery positions to 2011. Two of the New A330 Aircraft are scheduled to be delivered in 2010, six are scheduled to be delivered in 2011 and the remaining three are scheduled to be delivered in 2012.

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The following table sets forth certain information with respect to the aircraft owned by us as of June 30, 2009:  
**AIRCATTLE AIRCRAFT INFORMATION**

| <b>(Dollars in millions)</b>   | <b>Owned<br/>Aircraft as of<br/>June 30, 2009<sup>(1)</sup></b> |
|--|---|
| Flight Equipment Held for Lease  | \$ 3,832  |
| Number of Aircraft   | 131   |
| Number of Lessees  | 60  |
| Number of Countries  | 35  |
| Weighted Average Age Passenger (years) <sup>(2)(5)</sup>                     | 11.1  |
| Weighted Average Age Freighter (years) <sup>(2)(5)</sup>                     | 9.9   |
| Weighted Average Age Combined (years) <sup>(2)(5)</sup>                      | 10.7  |
| Weighted Average Remaining Passenger Lease Term (years) <sup>(3)(5)</sup>    | 3.6   |
| Weighted Average Remaining Cargo Lease Term (years) <sup>(3)(5)</sup>        | 8.1   |
| Weighted Average Remaining Combined Lease Term (years) <sup>(3)(5)</sup>     | 5.0   |
| Weighted Average Fleet Utilization during Second Quarter 2009 <sup>(4)</sup> | 98%   |

(1) Calculated using net book value as of June 30, 2009.

(2) Weighted average age (years) by net book value.

(3) Weighted average remaining lease term (years) by net book value.

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

(5) Four Boeing Model 737-400 aircraft which will be converted to freighter configuration are

included as  
 Freighter  
 aircraft; the  
 remaining lease  
 terms for these  
 aircraft, for  
 which we have  
 executed leases  
 post-conversion,  
 are measured  
 based on the  
 ten-year terms of  
 the  
 post-conversion  
 leases.

## PORTFOLIO DIVERSIFICATION

|                                 | <b>Owned Aircraft as of<br/>June 30, 2009</b> |                                    |
|---------------------------------|---|------------------------------------|
|                                 | <b>Number<br/>of<br/>Aircraft</b>             | <b>% of Net<br/>Book<br/>Value</b> |
| <b>Aircraft Type</b>            |   |                                    |
| Passenger:                      |   |                                    |
| Narrowbody                      | 86  | 45%                                |
| Midbody                         | 23  | 23%                                |
| Widebody                        | 1   | 2%                                 |
| Total Passenger                 | 110   | 70%                                |
| Freighter <sup>(1)</sup>        | 21  | 30%                                |
| <b>Total</b>                    | <b>131</b>                                    | <b>100%</b>                        |
| <b>Manufacturer</b>             |   |                                    |
| Boeing                          | 89  | 66%                                |
| Airbus                          | 42  | 34%                                |
| <b>Total</b>                    | <b>131</b>                                    | <b>100%</b>                        |
| <b>Regional Diversification</b> |   |                                    |
| Europe                          | 60  | 46%                                |
| Asia <sup>(1)</sup>             | 32  | 22%                                |
| North America                   | 14  | 12%                                |
| Latin America                   | 10  | 8%                                 |
| Middle East and Africa          | 15  | 12%                                |
| <b>Total</b>                    | <b>131</b>                                    | <b>100%</b>                        |



- (1) Includes four Boeing Model 737-400 aircraft which will be converted to freighter configuration as Freighter aircraft and for which we have executed leases with a carrier in Asia for delivery post-conversion.

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Our largest customer represents less than 8% of the net book value of flight equipment held for lease at June 30, 2009. Our top 15 customers for aircraft we owned at June 30, 2009, representing 54 aircraft and 58% of the net book value of flight equipment held for lease, are as follows:

| <b>Percent of Net Book Value</b> | <b>Customer</b>                       | <b>Country</b>       | <b>Number of Aircraft</b> |
|----------------------------------|---------------------------------------|----------------------|---------------------------|
| Greater than 6% per customer     | Martinair                             | Netherlands          | 5                         |
|                                  | Emirates                              | United Arab Emirates | 2                         |
|                                  | US Airways                            | USA                  | 8                         |
| 3% to 6% per customer            | Iberia Airlines                       | Spain                | 6                         |
|                                  | GOL Transportes Aereos <sup>(1)</sup> | Brazil               | 6                         |
|                                  | Airbridge Cargo <sup>(2)</sup>        | Russia               | 1                         |
|                                  | World Airways                         | USA                  | 2                         |
|                                  | KLM Royal Dutch Airlines              | Netherlands          | 1                         |
|                                  | Icelandair <sup>(3)</sup>             | Iceland              | 5                         |
| Less than 3% per customer        | Swiss International Air Lines         | Switzerland          | 2                         |
|                                  | China Eastern Airlines <sup>(4)</sup> | China                | 4                         |
|                                  | Jet Airways                           | India                | 4                         |
|                                  | Korean Air                            | South Korea          | 2                         |
|                                  | Cimber-Sterling                       | Denmark              | 4                         |
|                                  | SriLankan Airlines                    | Sri Lanka            | 2                         |

(1) VRG Linhas Aereas and GOL Transportes Aereos are shown combined in the above table.

(2) Guaranteed by Volga-Dnepr.

(3) Icelandair and SmartLynx are shown combined in the above table.

(4) China Eastern Airlines has announced that it will acquire Shanghai Airlines, a customer to

which we lease  
four aircraft.

The combined  
entity would be  
our 4<sup>th</sup> largest  
customer, with  
over 4% of net  
book value of  
flight equipment  
held for lease.

Our owned aircraft portfolio as of June 30, 2009 is listed in Exhibit 99.1 to this report. Approximately 87% of the total aircraft and 88% of the freighters we owned as of June 30, 2009 are what we consider to be the most current technology for the relevant airframe and engine type and airframe size, as listed under the headings Latest Generation Narrowbody Aircraft, Latest Generation Midbody Aircraft, Latest Generation Widebody Aircraft and Latest Generation Widebody Freighter Aircraft in Exhibit 99.1 to this report.

#### **Finance**

We have typically financed the initial purchase of aircraft using short-term credit arrangements and cash on hand. We then refinanced these short-term credit facilities on a long-term basis with the net proceeds from subsequent securitizations, bank debt and equity offerings. Our debt financing arrangements have been secured by the acquired aircraft and related leases, and the financing parties have limited recourse to Aircastle Limited. While such financing has historically been available on reasonable terms given the loan to value profile we have used, the current financial markets turmoil has significantly reduced the availability of both debt and equity capital and the terms on which any such capital may be made available to us would not be as favorable to us. Though we expect the financing market to improve in time, we are presently taking a cautious approach to incremental financing and with respect to refinancing risk.

To the extent that we acquire additional aircraft directly, we intend to fund such investments through medium to longer-term financings, including commercial and export credit agency supported debt, and cash on hand. We may repay all or a portion of such borrowings from time to time with the net proceeds from subsequent long-term debt financings, additional equity offerings or cash generated from operations and asset sales. Therefore, our ability to execute our business strategy, particularly the acquisition of additional commercial jet aircraft or other aviation assets, depends to a significant degree on our ability to obtain additional debt and equity capital on terms we deem attractive.

**Table of Contents****RESULTS OF OPERATIONS***Comparison of the three months ended June 30, 2008 to the three months ended June 30, 2009*

|   | <b>Three Months Ended<br/>June 30,</b> |             |
|---|--|-------------|
|   | <b>2008</b>                            | <b>2009</b> |
|   | <b>(Dollars in thousands)</b>          |             |
| Revenues:   |  |             |
| Lease rental revenue  | \$ 137,647                             | \$ 129,406  |
| Amortization of net lease discounts and lease incentives  | 2,502                                  | (2,810)     |
| Maintenance revenue   | 4,142                                  | 9,637       |
| <br>  |  |             |
| Total lease rentals   | 144,291                                | 136,233     |
| Interest income   | 614                                    | 594         |
| Other revenue   | 490                                    | 86          |
| <br>  |  |             |
| Total revenues  | 145,395                                | 136,913     |
| <br>  |  |             |
| Expenses:   |  |             |
| Depreciation  | 51,605                                 | 51,688      |
| Interest, net   | 51,319                                 | 41,482      |
| Selling, general and administrative (including non-cash share based payment expense of \$1,615 and \$1,729 for the three months ended June 30, 2008 and 2009, respectively) | 11,354                                 | 11,122      |
| Maintenance and other costs   | 597                                    | 4,502       |
| <br>  |  |             |
| Total operating expenses  | 114,875                                | 108,794     |
| <br>  |  |             |
| Other income:   |  |             |
| Gain on sale of aircraft  | 5,126                                  |             |
| Other   | 1,328                                  | 1,501       |
| <br>  |  |             |
| Total other income  | 6,454                                  | 1,501       |
| <br>  |  |             |
| Income from continuing operations before income taxes   | 36,974                                 | 29,620      |
| Income tax provision  | 1,633                                  | 2,049       |
| <br>  |  |             |
| Net income  | \$ 35,341                              | \$ 27,571   |

***Revenues:***

Total revenues decreased by 5.8% or \$8.5 million for the three months ended June 30, 2009 as compared to the three months ended June 30, 2008, primarily as a result of the following:

*Lease rental revenue.* The decrease in lease rental revenue of \$8.2 million for the three months ended June 30, 2009 as compared to the same period in 2008 was primarily the result of decreases of:

\$5.0 million of revenue downtime in connection with aircraft in transition and freighter conversions;

\$2.7 million of revenue as a result of the impact of 2008 and 2009 aircraft acquisitions net of dispositions; and

\$0.5 million due to lower floating rate lease rentals and lease rate changes.

*Amortization of net lease discounts and lease incentives.* The decrease in amortization of net lease discounts and lease incentives of \$5.3 million for the three months ended June 30, 2009 as compared to the same period in 2008 results from the decrease in amortization of net lease discounts of \$1.2 million and an increase in amortization of lease incentives of \$4.1 million for aircraft transitions.

*Maintenance revenue.* The increase in maintenance revenue of \$5.5 million is primarily the result of \$1.0 million of maintenance revenue from scheduled lease terminations (\$5.2 million in the three months ended June 30, 2009 as compared to \$4.1 million in the three months ended June 30, 2008) and \$4.5 million of maintenance revenue from early terminations of leases in the three months ended June 30, 2009.

**Table of Contents****Operating Expenses:**

Total operating expenses decreased by 5% or \$6.1 million for the three months ended June 30, 2009 as compared to the three months ended June 30, 2008 primarily as a result of the following:

*Depreciation expense* increased by \$0.1 million for the three months ended June 30, 2009 over the same period in 2008 as a result of an increase in the aircraft book value due to the aircraft acquired in 2008, partially offset by the reduction in depreciation expense as a result of the sales of owned aircraft in 2008.

*Interest, net* consisted of the following:

|  | <b>Three Months Ended<br/>June 30,</b> |             |
|--|--|-------------|
|  | <b>2008</b>                            | <b>2009</b> |
|  | <b>(Dollars in thousands)</b>          |             |
| Interest on borrowings and other liabilities                                 | \$ 46,171                              | \$ 36,642   |
| Hedge ineffectiveness (gains) losses (unrealized)                            | 3,907                                  | (3,202)     |
| Amortization of interest rate derivatives related to deferred (gains) losses | 687                                    | 2,847       |
| (Gain) losses on termination of interest rate derivatives                    | (18)                                   | 2,758       |
| Amortization of deferred financing fees                                      | 4,203                                  | 3,198       |
| Interest Expense   | 54,950                                 | 42,243      |
| Less interest income   | (2,827)                                | (416)       |
| Less capitalized interest  | (804)                                  | (345)       |
| Interest, net  | \$ 51,319                              | \$ 41,482   |

Interest, net decreased by \$9.8 million, or 19%, over the three months ended June 30, 2008. The net decrease is primarily a result of:

a \$9.5 million decrease in interest expense on our borrowings primarily due to a lower average debt balance;

a \$7.1 million decrease resulting from changes in measured hedge ineffectiveness; and

a \$1.0 million decrease in amortization of deferred financing fees resulting primarily from the write-off of fees during the second quarter of 2008.

These decreases were partially offset by:

a \$2.2 million increase in amortization of deferred losses due to the termination of several interest rate derivative contracts during the fourth quarter of 2008;

a \$2.8 million hedge termination charge in the second quarter of 2009;

a \$2.4 million decrease in interest income, reflecting significantly lower interest rates during the second quarter of 2009 compared to the same period in 2008; and

a \$0.5 million decrease in capitalized interest due to delivery of aircraft from freighter conversion and lower interest rates during the second quarter of 2009 compared to the same period in 2008.

*Selling, general and administrative expenses, or SG&A*, for the three months ended June 30, 2009 decreased by \$0.2 million, or 2% over the same period in 2008. This decrease was due mainly to a decrease in personnel costs of \$0.5 million and travel expenses of \$0.1 million, partially offset by an increase in professional fees of \$0.4 million. Non-cash share based expense was \$1.6 million in 2008 and \$1.7 million in 2009, respectively.

*Maintenance and other costs* increased \$3.9 million primarily as a result of aircraft transition costs for six of the eight aircraft returned from bankrupt lessees and three aircraft with leases that terminated before scheduled expiry.



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***Other income:***

Total other income for the three months ended June 30, 2009 decreased by \$5.0 million over the same period in 2008 primarily as a result of the gain on sale of aircraft of \$5.1 million recorded during the second quarter of 2008.

***Income Tax Provision***

Our provision for income taxes for the three months ended June 30, 2008 and 2009 was \$1.6 million and \$2.0 million, respectively. Income taxes have been provided based on the applicable tax laws and rates of those countries in which operations are conducted and income is earned, primarily Ireland and the United States. The increase in our income tax provision of approximately \$0.4 million for the three months ended June 30, 2009 as compared to the same period in 2008 was primarily attributable to the increase in our operating income subject to tax in Ireland and the United States.

All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes, unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. We also have a U.S.-based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes.

The Company received an assurance from the Bermuda Minister of Finance that it would be exempted from local income, withholding and capital gains taxes until March 2016. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily the United States and Ireland.



**Table of Contents****Comparison of the six months ended June 30, 2008 to the six months ended June 30, 2009**

|   | <b>Six Months Ended<br/>June 30,</b> |             |
|---|--------------------------------------|-------------|
|   | <b>2008</b>                          | <b>2009</b> |
|   | <b>(Dollars in thousands)</b>        |             |
| <b>Revenues:</b>  |                                      |             |
| Lease rental revenue  | \$ 268,628                           | \$ 255,400  |
| Amortization of net lease discounts and lease incentives  | 5,148                                | (3,927)     |
| Maintenance revenue   | 4,142                                | 16,240      |
| <br>  |                                      |             |
| Total lease rentals   | 277,918                              | 267,713     |
| Interest income   | 1,905                                | 1,227       |
| Other revenue   | 528                                  | 111         |
| <br>  |                                      |             |
| Total revenues  | 280,351                              | 269,051     |
| <br>  |                                      |             |
| <b>Expenses:</b>  |                                      |             |
| Depreciation  | 99,820                               | 103,249     |
| Interest, net   | 92,330                               | 84,893      |
| Selling, general and administrative (including \$3,213 and \$3,387 for the six months ended June 30, 2008 and 2009, respectively) | 22,843                               | 22,217      |
| Maintenance and other costs   | 1,242                                | 10,278      |
| <br>  |                                      |             |
| Total operating expenses  | 216,235                              | 220,637     |
| <br>  |                                      |             |
| <b>Other income:</b>  |                                      |             |
| Gain on sale of aircraft  | 5,126                                |             |
| Other   | 1,083                                | 1,593       |
| <br>  |                                      |             |
| Total other income  | 6,209                                | 1,593       |
| <br>  |                                      |             |
| Income from continuing operations before income taxes   | 70,325                               | 50,007      |
| Income tax provision  | 3,347                                | 3,965       |
| <br>  |                                      |             |
| Net income  | \$ 66,978                            | \$ 46,042   |

**Revenues:**

Total revenues decreased by 4.0% or \$11.3 million for the six months ended June 30, 2009 as compared to the six months ended June 30, 2008, primarily as a result of the following:

*Lease rental revenue.* The decrease in lease rental revenue of \$13.2 million for the six months ended June 30, 2009 as compared to the same period in 2008 was primarily the result of decreases of:

\$12.5 million of revenue downtime in connection with aircraft in transition and freighter conversions; and

\$1.5 million due to lower floating rate lease rentals and lease rate changes.

These decreases were partially offset by:

\$0.8 million of additional revenue as a result of the impact of 2008 and 2009 aircraft acquisitions net of dispositions.

*Amortization of net lease discounts and lease incentives.* The decrease in amortization of net lease discounts and lease incentives of \$9.1 million for the six months ended June 30, 2009 as compared to the same period in 2008 results from the decrease in amortization of net lease discounts of \$2.4 million and an increase in amortization of lease incentives of \$6.7 million for aircraft transitions.

*Maintenance revenue.* The increase in maintenance revenue of \$12.1 million is primarily the result of \$5.1 million of maintenance revenue from scheduled lease terminations (\$9.2 million in the six months ended June 30, 2009 as compared to \$4.1 million in the six months ended June 30, 2008) and \$7.0 million of maintenance revenue from early terminations of leases in the six months ended June 30, 2009.

*Interest Income.* The decrease in interest income of \$0.7 million was primarily due to the sale of two of our debt investments in February 2008.

**Table of Contents****Operating Expenses:**

Total operating expenses increased by 2% or \$4.4 million for the six months ended June 30, 2009 as compared to the six months ended June 30, 2008 primarily as a result of the following:

*Depreciation expense* increased by \$3.4 million for the six months ended June 30, 2009 over the same period in 2008 as a result of an increase in the aircraft book value due to the aircraft acquired in 2008, partially offset by the reduction in depreciation expense as a result of the sales of owned aircraft in 2008.

*Interest, net* consisted of the following:

|  | <b>Six Months Ended<br/>June 30,</b> |             |
|--|--------------------------------------|-------------|
|  | <b>2008</b>                          | <b>2009</b> |
|  | <b>(Dollars in thousands)</b>        |             |
| Interest on borrowings and other liabilities                                 | \$ 88,050                            | \$ 73,412   |
| Hedge ineffectiveness (gains) losses (unrealized)                            | 5,905                                | (3,331)     |
| Amortization of interest rate derivatives related to deferred (gains) losses | (473)                                | 7,796       |
| Losses on termination of interest rate derivatives                           | 1,003                                | 2,758       |
| Amortization of deferred financing fees                                      | 6,787                                | 5,731       |
| Interest Expense   | 101,272                              | 86,366      |
| Less interest income   | (4,558)                              | (857)       |
| Less capitalized interest  | (4,384)                              | (616)       |
| Interest, net  | \$ 92,330                            | \$ 84,893   |

Interest, net decreased by \$7.4 million, or 8%, over the six months ended June 30, 2008. The net decrease is primarily a result of:

a \$14.6 million decrease in interest expense on our borrowings primarily due to a lower average debt balance;

a \$9.2 million decrease resulting from changes in measured hedge ineffectiveness; and

a \$1.1 million decrease in amortization of deferred financing fees resulting primarily from the write-off of fees during the second quarter of 2008.

These decreases were partially offset by:

a \$8.3 million increase in amortization of deferred losses primarily due to the termination of several interest rate derivative contracts during the fourth quarter of 2008;

a \$1.8 million increase in hedge termination charges;

a \$3.7 million decrease in interest income, reflecting significantly lower interest rates during the six months ended June 30, 2009 compared to the same period in 2008; and

a \$3.8 million decrease in capitalized interest due to delivery of aircraft from freighter conversion and lower interest rates during six months ended June 30, 2009 compared to the same period in 2008.

*Selling, general and administrative expenses, or SG&A*, for the six months ended June 30, 2009 decreased by \$0.6 million, or 3% over the same period in 2008. This decrease was due mainly to a decrease in personnel costs of \$0.8 million, partially offset by an increase in professional fees of \$0.1 million. Non-cash share based expense was \$3.2 million in 2008 and \$3.4 million in 2009, respectively.

*Maintenance and other costs* increased \$9.0 million primarily as a result of aircraft transition costs for six of the eight aircraft returned from bankrupt lessees and three aircraft with leases that terminated before scheduled expiry.

***Other income:***

Total other income for the six months ended June 30, 2009 decreased by \$4.6 million over the same period in 2008 primarily as a result of the gain on sale of aircraft of \$5.1 million recorded during the second quarter of 2008.

**Table of Contents*****Income Tax Provision***

Our provision for income taxes for the six months ended June 30, 2008 and 2009 was \$3.3 million and \$4.0 million, respectively. Income taxes have been provided based on the applicable tax laws and rates of those countries in which operations are conducted and income is earned, primarily Ireland and the United States. The increase in our income tax provision of approximately \$0.6 million for the six months ended June 30, 2009 as compared to the same period in 2008 was primarily attributable to the increase in our operating income subject to tax in Ireland and the United States.

All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes, unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. We also have a U.S.-based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes.

The Company received an assurance from the Bermuda Minister of Finance that it would be exempted from local income, withholding and capital gains taxes until March 2016. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily the United States and Ireland.

**RECENT ACCOUNTING PRONOUNCEMENTS**

Effective January 1, 2009, the Company adopted Financial Accounting Standards Board ( FASB ) Statement of Accounting Standards ( SFAS ) No. 161, *Disclosures about Derivative Instruments and Hedging Activities*, an amendment of FASB Statement No. 133 *Accounting for Derivative Instruments and Hedging Activities*, or SFAS No. 161. SFAS No. 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows.

Also effective January 1, 2009, the Company adopted FASB Staff Position ( FSP ) No. EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities*, or FSP No. EITF 03-6-1. FSP No. EITF 03-6-1 addresses whether unvested share-based payment awards with rights to receive dividends or dividend equivalents should be considered participating securities for the purposes of applying the two-class method of calculating earnings per share ( EPS ) under SFAS No. 128, *Earnings per Share*. The FASB staff concluded that unvested share-based payment awards that contain rights to receive nonforfeitable dividends or dividend equivalents (whether paid or unpaid) are participating securities, and thus, should be included in the two-class method of computing EPS. The adoption of FSP No. EITF 03-6-1 requires us to present EPS using the two-class method for our current period EPS computations and to retrospectively revise our comparative prior period EPS computations using the two-class method. The adoption of FSP No. EITF 03-6-1 did not have a material effect on EPS.

In April, 2009, the FASB issued three final FSPs intended to provide additional application guidance and enhance disclosures regarding fair value measurements and impairments of securities. FSP No. FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, provides guidelines for making fair value measurements more consistent with the principles presented in FASB Statement No. 157, *Fair Value Measurements*. FSP No. FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*, enhances consistency in financial reporting by increasing the frequency of fair value disclosures. FSP FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*, provides additional guidance designed to create greater clarity and consistency in accounting for and presenting impairment losses on securities. The FSPs are effective for interim and annual periods ending after June 15, 2009, but entities may early adopt the FSPs for the interim and annual periods ending after March 15, 2009. The Company adopted these FSPs during the second quarter of 2009 and the adoption of these FSPs did not have a material impact on our consolidated financial statements.

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In May 2009, the FASB issued SFAS No. 165, *Subsequent Events*, or SFAS No. 165. SFAS No. 165 is intended to establish general standards of accounting for, and disclosure of, events that occur after the balance sheet date but before financial statements are issued or are available to be issued. It requires the disclosure of the date through which an entity has evaluated subsequent events and the basis for that date that is, whether that date represents the date the financial statements were issued or were available to be issued. SFAS No. 165 is effective for interim and annual periods ending after June 15, 2009. The Company adopted SFAS No. 165 during the second quarter of 2009 and the adoption of SFAS No. 165 did not have a material impact on our consolidated financial statements.

In June 2009, the FASB issued SFAS No. 167, *Amendments to FASB Interpretation (FIN) No. 46(R)* (SFAS No. 167), which amends FIN No. 46(R) to require an enterprise to perform an analysis to determine whether the enterprise's variable interest, or interests, give it a controlling financial interest in a variable interest entity. The determination of whether a reporting entity is required to consolidate another entity is based on, among other things, the other entity's purpose and design and the reporting entity's ability to direct the activities of the other entity that most significantly impact the other entity's economic performance. This Statement amends certain guidance in FIN No. 46(R) for determining whether an entity is a variable interest entity and requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity. SFAS No. 167 will require a reporting entity to provide additional disclosures about its involvement with variable interest entities and any significant changes in risk exposure due to that involvement. SFAS No. 167 will be effective for fiscal years beginning after November 15, 2009, and interim periods within those fiscal years. The Company is currently evaluating the requirements of SFAS No. 167 and has not yet determined the impact on the Company's consolidated financial statements.

Also in June 2009, the FASB issued SFAS No. 168, *The FASB Accounting Standards Codification<sup>TM</sup> (Codification) and the Hierarchy of Generally Accepted Accounting Principles, a replacement of FASB Statement No. 162*, or SFAS No. 168. This Statement replaces FASB Statement No. 162, *The Hierarchy of Generally Accepted Accounting Principles* and identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP in the United States (the GAAP hierarchy). Rules and interpretive releases of the SEC under federal securities laws are also sources of authoritative GAAP for SEC registrants. The Codification does not replace or affect guidance issued by the SEC or its staff for public entities in their filings with the SEC. SFAS No. 168 shall be effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Company plans to adopt SFAS No. 168 during the third quarter of 2009 and the adoption of SFAS No. 165 is not expected to have a material effect on our consolidated financial statements.

**LIQUIDITY AND CAPITAL RESOURCES**

We have been able to meet our liquidity and capital resource requirements by utilizing several sources, including: lines of credit, our securitizations, term financings, and other secured borrowings;

our public offerings of common shares;

prior to our initial public offering, equity contributions from funds managed by affiliates of Fortress;

aircraft lease revenues and maintenance payments;

principal and interest payments from our debt investments; and

asset sales.

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During the six months ended June 30, 2009, we acquired an aircraft and made capital expenditures (including lease incentives) to our aircraft portfolio totaling \$105.7 million. We expect to fund approximately \$136.4 million of purchase obligations for aircraft pre-delivery and conversion payments during the next twelve months. In addition, at June 30, 2009, we expect capital expenditures and lessee maintenance payment draws on our owned and committed aircraft portfolio to be approximately \$105 million to \$115 million, excluding freighter conversion payments (see Purchase Obligations in Contractual Obligations below), and we expect maintenance payment collections from lessees on our owned aircraft portfolio of approximately equal to the expected expenditures and draws over the next twelve months. There can be no assurance that the capital expenditures, our contributions to maintenance events and lessee maintenance payment draws described above will not be greater than expected or that our expected maintenance payment collections or disbursements will equal our current estimates.

We believe that cash on hand and funds generated from operations will be sufficient to satisfy our liquidity needs, including our pre-delivery payments, required debt amortization, expected capital expenditures and lessor contributions over the next twelve months. In addition, potential asset sales and an anticipated future financing facility to fund a portion of the Airbus pre-delivery payments may provide additional sources of liquidity over that time frame.

**Cash Flows**

|  | <b>Six Months Ended<br/>June 30,</b> |             |
|--|--------------------------------------|-------------|
|  | <b>2008</b>                          | <b>2009</b> |
|  | <b>(Dollars in thousands)</b>        |             |
| Net cash flow provided by operating activities | \$137,188                            | \$ 126,491  |
| Net cash flow used in investing activities     | (80,164)                             | (144,735)   |
| Net cash flow provided by financing activities | 6,377                                | 33,082      |

Operating activities provided net cash flow of \$137.2 million and \$126.5 million for the six months ended June 30, 2008 and June 30, 2009, respectively. Net cash from operations decreased \$10.7 million for the six months ended June 30, 2009 versus the same period in 2008 primarily as a result of:

\$13.2 million decrease in cash flow from lease rental revenues;

\$0.2 million decrease in cash flow from working capital (changes in certain assets and liabilities); and

\$9.0 million cash paid for aircraft transition costs in 2009.

These decreases were partially offset by:

\$7.9 million decrease in cash payments for interest; and

\$6.4 million increase in cash received for maintenance revenue.

Net cash flow used in investing activities was \$80.2 million and \$144.7 million for the six months ended June 30, 2008 and June 30, 2009, respectively. Net cash used in investing activities for the six months ended June 30, 2009 consisted primarily of:

\$105.7 million of cash used for aircraft acquisitions and capital expenditures (including lease incentives); and

\$39.7 million of cash used for aircraft pre-delivery payments and progress payments on conversions of aircraft.

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Net cash flow provided by financing activities totaled \$6.4 million for the six months ended June 30, 2008 and \$33.1 million for the six months ended June 30, 2009. The net increase in cash flow provided by financing activities of \$26.7 million versus the same period in 2008 was a result of:

\$67.8 million of lower principal repayments on our repurchase agreements;

\$65.6 million of lower payments for terminated cash flow hedges;

\$58.9 million of lower dividend payments;

\$14.5 million of lower deferred financings costs; and

\$7.5 million of security deposits and maintenance payments received (net of payments).

These increases were partially offset by:

\$188.6 million of lower borrowings (net of repayments) on our credit facilities, term debt financings and securitizations.

**Debt Obligations**

The following table provides a summary of our securitizations and term financing facilities at June 30, 2009:

| <b>Debt Obligation</b> | <b>Collateral</b>   | <b>Outstanding<br/>Borrowing<sup>(1)</sup><br/>(Dollars in thousands)</b> | <b>Number<br/>of<br/>Aircraft</b> | <b>Interest<br/>Rate<sup>(2)</sup></b> | <b>Final<br/>Stated<br/>Maturity<sup>(3)</sup></b> |
|------------------------|---|---|-----------------------------------|--|--|
| Securitization No. 1   | Interests in aircraft leases, beneficial interests in aircraft owning entities and related interests  | \$ 461,324  | 36                                | 0.59%                                  | 6/20/31  |
| Securitization No. 2   | Interests in aircraft leases, beneficial interests in aircraft owning entities and related interests  | 1,082,486   | 57                                | 0.58%                                  | 6/14/37  |
| Term Financing No. 1   | Interests in aircraft leases, beneficial interests in aircraft owning entities and related interests  | 733,160   | 28                                | 2.08%                                  | 5/02/15  |
| Term Financing No. 2   | Interests in aircraft leases, beneficial interests in aircraft owning entities and related interests  | 133,852   | 8                                 | 3.30%                                  | 9/23/13  |
| ECA Term Financing     | Interests in aircraft leases, beneficial interests in aircraft leasing entities and related interests | 70,543  | 1                                 | 4.48%                                  | 5/27/21  |
| Total                  |   | \$ 2,481,365  |                                   |  |  |

(1) Outstanding borrowing amount equals



committed  
borrowing  
amount at  
June 30, 2009.

- (2) Reflects floating rate in effect at the most recent applicable reset date.
- (3) For Securitization No. 1, Securitization No. 2 and Term Financing No. 1, all cash flows available after expenses and interest will be applied to debt amortization, if the debt is not refinanced by June 2011, June 2012, and May 2013, respectively.

Our debt obligations contain various loan covenants which are customary for financings of the relevant type. Such covenants do not, in management's opinion, materially restrict our investment strategy or our ability to raise capital. We are in compliance with all of our loan covenants as of June 30, 2009.

In May 2009, we entered into a twelve-year \$70.9 million term loan with Citibank International Plc which is supported by a guarantee from Compagnie Francaise d'Assurance pour le Commerce Exterieur, or COFACE, the French government sponsored export credit agency, or ECA, which we refer to as ECA Term Financing for the financing of a new Airbus Model A330-200 aircraft. The borrowing under the ECA Term Financing bears a fixed rate of interest equal to 4.475%. The obligations outstanding under the ECA Term Financing are secured by, among other things, a mortgage over the aircraft and a pledge of our ownership interest in our subsidiary company that leases the aircraft to the operator. The ECA Term Financing documents contain a \$500 million minimum net worth covenant for Aircastle Limited, as well as a material adverse change default and cross default to any other recourse obligation of

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Aircastle Limited, and other terms and conditions customary for ECA-supported financings being completed at this time. In addition, Aircastle Limited has guaranteed the repayment of the ECA Term Financing.

The following securitizations and term debt financing structures include liquidity facility commitments described in the table below:

| Facility             | Liquidity Facility Provider | Available Liquidity |                       | Unused Fee | Interest Rate on any Advances   |
|----------------------|-----------------------------|---------------------|-----------------------|------------|---------------------------------|
|                      |                             | December 31, 2008   | June 30, 2009         |            |                                 |
| Securitization No. 1 | Calyon                      | \$42,000            | \$42,000              | 0.45%      | 1M Libor + 1.00%                |
| Securitization No. 2 | HSH Nordbank AG             | 82,343              | 81,186 <sup>(1)</sup> | 0.50%      | 1M Libor + 0.75% <sup>(2)</sup> |
| Term Financing No. 1 | Calyon                      | 15,152              | 14,663                | 0.60%      | 1M Libor + 1.20%                |

(1) Following a ratings downgrade with respect to the liquidity facility provider in May 2009, the liquidity facility was drawn and the proceeds, or permitted investments thereof, remain available to provide liquidity if required.

(2) Amounts drawn following a ratings downgrade with respect to the liquidity facility provider do not bear interest; however, net investment earnings will be paid to the liquidity facility provider and the unused fee continues to apply.

The purpose of these facilities is to provide liquidity for the relevant securitization or term financing in the event that cash flow from lease contracts and other revenue sources is not sufficient to pay operating expenses with respect to the relevant aircraft portfolio and interest payments and interest rate hedging payments for the relevant securitization or term debt financings. These liquidity facilities are generally 364-day commitments of the liquidity provider and may be extended prior to expiry. If a facility is not extended, or in certain circumstances if the short-term credit rating of the liquidity provider is downgraded, the relevant securitization or term financing documents require that the liquidity facility is drawn and the proceeds of the drawing placed on deposit so that such amounts may be available, if needed, to provide liquidity advances for the relevant securitization or term financing. Downgrade or non-extension drawings are generally not required to be repaid to the liquidity facility provider until 15 days after final maturity of the securitization or term financing debt. In the case of the liquidity facilities for Securitization No. 2 and Term Financing No. 1, the required amount of the facilities reduce over time as the principal balance of the debt amortizes, with the Securitization No. 2 liquidity facility having a minimum required amount of \$65 million.

In May 2009, we were notified of a short-term credit rating downgrade of the liquidity facility provider for Securitization No. 2, HSH Nordbank AG. This downgrade required a drawing of the liquidity facility in cash, which was deposited in a liquidity facility deposit account and held as cash collateral. In June 2009, HSH Nordbank AG directed the investment of this cash into a long-term, AAA-rated investment. We returned the cash in exchange for the long-term investment, which was considered a non-cash transaction and accordingly, at June 30, 2009, an amount of \$81.2 million is recorded as an asset on our consolidated balance sheet as Restricted liquidity facility collateral. In addition, the commitment to repay the Securitization No. 2 liquidity facility in the amount of \$81.2 million is recorded as a liability on our consolidated balance sheet as Liquidity facility. As of June 30, 2009, the liquidity facilities for Securitization No. 1 and Term Financing No. 1 remain undrawn.

#### **Contractual Obligations**

Our contractual obligations consist of principal and interest payments on variable rate liabilities, obligations under the Airbus A330 Agreement, obligations under our freighter conversion contracts and rent payments pursuant to our office leases. Total contractual obligations decreased from \$3.75 billion at December 31, 2008 to approximately \$3.45 billion at June 30, 2009 due primarily to principal and interest payments made under our securitizations and term financings, lower variable interest rates and payments made under our purchase obligations.

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The following table presents our actual contractual obligations and their payment due dates as of June 30, 2009:

| Contractual Obligations             | Total               | Payments Due By Period as of June 30, 2009 |                     |                   |                     |
|-------------------------------------|---------------------|--|---------------------|-------------------|---------------------|
|                                     |                     | Less than                                  |                     |                   | More than           |
|                                     |                     | 1 year                                     | 2-3 years           | 4-5 years         | 5 years             |
|                                     |                     | <b>(Dollars in thousands)</b>              |                     |                   |                     |
| Securitization No. 1 <sup>(1)</sup> | \$ 472,059          | \$ 24,929                                  | \$ 124,685          | \$ 193,629        | \$ 128,816          |
| Securitization No. 2 <sup>(2)</sup> | 1,114,966           | 56,666                                     | 123,488             | 346,342           | 588,470             |
| Term Financing No. 1 <sup>(3)</sup> | 804,885             | 63,890                                     | 124,720             | 187,534           | 428,741             |
| Term Financing No. 2 <sup>(4)</sup> | 143,837             | 34,831                                     | 70,977              | 38,029            |                     |
| ECA Term Financing <sup>(5)</sup>   | 91,144              | 7,648                                      | 15,297              | 15,297            | 52,902              |
| Office leases <sup>(6)</sup>        | 4,177               | 1,041                                      | 1,971               | 785               | 380                 |
| Purchase obligations <sup>(7)</sup> | 817,791             | 136,410                                    | 681,381             |                   |                     |
| <b>Total</b>                        | <b>\$ 3,448,859</b> | <b>\$ 325,415</b>                          | <b>\$ 1,142,519</b> | <b>\$ 781,616</b> | <b>\$ 1,199,309</b> |

(1) Includes interest on variable rate, LIBOR-based instruments at the June 30, 2009 rate and principal payments based on amortization schedules through October 2015 that require the securitization cash flows be applied to the outstanding principal balance of the indebtedness so that the loan to assumed aircraft values are held constant through June 2011, after which all excess cash flow is required to reduce the principal balances of the indebtedness.

- (2) Includes interest on variable rate, LIBOR-based instruments at the June 30, 2009 rate and principal payments based on amortization schedules through February 2018 that require the securitization cash flows be applied to the outstanding principal balance of the indebtedness so that the loan to assumed aircraft values are held constant through June 2012, after which all excess cash flow is required to reduce the principal balances of the indebtedness. The Less than 1 year commitments include repayment of \$8.3 million and the 2-3 years commitments include repayments of \$15.2 million related to contracted sales for two aircraft in 2010 and one aircraft in 2011.

(3)

Includes interest on variable rate, LIBOR-based instruments at the June 30, 2009 rate and scheduled principal payments through May 2013, after which all excess cash flow is required to reduce the principal balances of the indebtedness until maturity in May 2015.

- (4) Includes interest on variable rate, LIBOR-based instruments at the June 30, 2009 rate and principal payments equal to 85% of the cash flow remaining after the payment of expenses, fees, interest and amounts owing to interest rate hedge providers.
- (5) Includes scheduled principal and interest payments based upon a fixed rate, 12 year, fully amortizing loan.
- (6) Represents contractual

payment obligations for our office leases in Stamford, Connecticut; Dublin, Ireland and Singapore.

- (7) At June 30, 2009, we had aircraft purchase agreements and freighter conversion agreements, including the acquisition of 11 New A330 Aircraft from Airbus. In July 2009, we amended the Airbus A330 Agreement to defer the scheduled delivery of an aircraft from 2010 to 2011. As a result, our committed amounts to acquire, convert and modify aircraft including, where applicable, our estimate of adjustments for configuration changes, engine acquisition costs, contractual price escalations and other adjustments, net of amounts already paid, will be

approximately  
\$818.9 million  
(\$123.6 million  
- less than one  
year and \$695.3  
million - 2-3  
years).

### **Capital Expenditures**

We make capital expenditures from time to time in connection with improvements made to our aircraft. These expenditures include the cost of major overhauls necessary to place an aircraft in service and modifications made at the request of lessees. For the six months ended June 30, 2008 and 2009, we incurred a total of \$19.2 million and \$24.7 million, respectively, of capital expenditures (including lease incentives) related to the acquisition and improvement of aircraft.

As of June 30, 2009, the weighted average age (by net book value) of our aircraft was approximately 10.7 years. In general, the costs of operating an aircraft, including maintenance expenditures, increase with the age of the aircraft. Under our leases, the lessee is primarily responsible for maintaining the aircraft. We may incur additional maintenance and modification costs in the future in the event we are required to remarket an aircraft or a lessee fails to meet its maintenance obligations under the lease agreement. At June 30, 2009, we had \$241.1 million of maintenance reserves as a liability on our balance sheet. These maintenance reserves are paid by the lessee to provide for future maintenance events. Provided a lessee performs scheduled maintenance of the aircraft, we are required to reimburse the lessee for scheduled maintenance payments. In certain cases, we are also required to make lessor contributions, in excess of amounts a lessee may have paid, towards the costs of maintenance events performed by or on behalf of the lessee.

Actual maintenance payments to us by lessees in the future may be less than projected as a result of a number of factors, including defaults by the lessees. Maintenance reserves may not cover the entire amount of actual maintenance expenses incurred and, where these expenses are not otherwise covered by the lessees, there can be no assurance that



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our operational cash flow and maintenance reserves will be sufficient to fund maintenance requirements, particularly as our aircraft age.

**Off-Balance Sheet Arrangements**

We did not have any off-balance sheet arrangements as of June 30, 2009.

**Foreign Currency Risk and Foreign Operations**

At June 30, 2009, all of our leases are payable to us in U.S. dollars. However, we incur Euro and Singapore dollar-denominated expenses in connection with our subsidiary in Ireland and branch office in Singapore. As of June 30, 2009, 11 of our 74 employees were based in Ireland and four employees were based in Singapore. For the six months ended June 30, 2009, expenses, such as payroll and office costs, denominated in currencies other than the U.S. dollar aggregated approximately \$3.5 million in U.S. dollar equivalents and represented approximately 16% of total selling, general and administrative expenses. Our international operations are a significant component of our business strategy and permit us to more effectively source new aircraft, service the aircraft we own and maintain contact with our lessees. Therefore, it is likely that our international operations and our exposure to foreign currency risk will increase over time. Although we have not yet entered into foreign currency hedges because our exposure to date has not been significant, if our foreign currency exposure increases we may enter into hedging transactions in the future to mitigate this risk. For the six months ended June 30, 2008 and 2009, we incurred insignificant net gains and losses on foreign currency transactions.

**Hedging**

In the normal course of business we utilize interest rate derivatives to manage our exposure to interest rate risks. Specifically, our interest rate derivatives are hedging variable rate interest payments on our various debt facilities. We account for our interest rate derivatives in accordance with Statement of Financial Accounting Standards, or SFAS, No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended and interpreted, or SFAS No. 133. Under SFAS No. 133, if certain conditions are met, an interest rate derivative may be specifically designated as a cash flow hedge. All of our designated interest rate derivatives are cash flow hedges. We have one interest rate derivative that is not designated under SFAS No. 133.

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We held the following derivative contracts as of June 30, 2009:

| Hedged Item  | Liability Derivatives |                |                |                 |                  |                | Balance Sheet Location               | Fair Value |
|--|-----------------------|----------------|----------------|-----------------|------------------|----------------|--------------------------------------|------------|
|  | Current               |                | Future Maximum |                 | Floating Rate    | Fixed Rate     |                                      |            |
|  | Notional Amount       | Effective Date | Maturity Date  | Notional Amount |                  |                |                                      |            |
|  |                       |                |                |                 |                  |                |                                      |            |
| <b>Interest rate derivatives designated as cash flow hedges under Statement 133:</b>     |                       |                |                |                 |                  |                |                                      |            |
| Securitization No. 1   | \$ 461,324            | Jun-06         | Jun-16         | \$ 461,324      | 1M LIBOR + 0.27% | 5.78%          | Fair value of derivative liabilities | \$ 54,121  |
| Securitization No. 2   | 1,073,895             | Jun-07         | Jun-12         | 1,073,895       | 1M LIBOR         | 5.25% to 5.36% | Fair value of derivative liabilities | 95,328     |
| Term Financing No. 1 <sup>(1)</sup>  | 665,658               | Jun-08         | May-13         | 665,658         | 1M LIBOR         | 4.04%          | Fair value of derivative liabilities | 34,664     |
| Term Financing No. 1 <sup>(1)</sup>  |                       | May-13         | May-15         | 491,718         | 1M LIBOR         | 5.31%          | Fair value of derivative liabilities | 4,176      |
| Total interest rate derivatives designated as cash flow hedges under Statement 133       | 2,200,877             |                |                | 2,692,595       |                  |                |                                      | 188,289    |
| <b>Interest rate derivatives not designated as cash flow hedges under Statement 133:</b> |                       |                |                |                 |                  |                |                                      |            |
| Term Financing No. 2 <sup>(2)</sup>  | 119,870               | Oct-08         | Sep-13         | 119,870         | 3M LIBOR         | 3.17%          | Fair value of derivative liabilities | 3,122      |
| Total interest rate derivatives not  | 119,870               |                |                | 119,870         |                  |                |                                      | 3,122      |

designated as  
cash flow hedges  
under Statement  
133

|                                 |              |              |            |
|---------------------------------|--------------|--------------|------------|
| Total interest rate derivatives | \$ 2,320,747 | \$ 2,812,465 | \$ 191,411 |
|---------------------------------|--------------|--------------|------------|

(1) The interest payments related to Term Financing No. 1 are being hedged by two consecutive interest rate derivatives. When the first matures in May 2013, the next becomes effective.

(2) Although we entered into this interest rate derivative to hedge the variable rate interest payments in connection with Term Financing No. 2, it has not been designated as a hedge for accounting purposes.

As of June 30, 2009, accrued interest payable included in Accounts payable, accrued expenses, and other liabilities on our consolidated balance sheet was \$5.9 million related to interest rate derivatives designated as cash flow hedges and \$68 thousand for interest rate derivatives not designated as cash flow hedges.

The amount of loss expected to be reclassified from accumulated OCI into interest expense over the next 12 months consists of net interest settlements on active interest rate derivatives disclosed above, in the amount of \$91.9 million and the amortization of deferred net losses in the amount of \$7.9 million. For the six months ended June 30, 2009, the amount of loss reclassified from accumulated OCI into interest expense consisted of net interest settlements on active interest rate derivatives in the amount of \$49.2 million, and the amortization of deferred net losses in the amount of \$4.1 million as disclosed below.

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The following table summarizes amounts charged directly to the consolidated statement of income for the three and six months ended June 30, 2008 and 2009, respectively, related to our interest rate derivatives:

|   | <b>Three Months<br/>Ended<br/>June 30,</b> |             | <b>Six Months Ended<br/>June 30,</b> |             |
|---|--|-------------|--------------------------------------|-------------|
|   | <b>2008</b>                                | <b>2009</b> | <b>2008</b>                          | <b>2009</b> |
|   | <b>(Dollars in thousands)</b>              |             |                                      |             |
| <b>Interest Expense:</b>  |  |             |                                      |             |
| Hedge ineffectiveness (gains) losses (unrealized)                       | \$ 3,907                                   | \$ (3,202)  | \$ 5,905                             | \$ (3,331)  |
| Amortization:   |  |             |                                      |             |
| Accelerated amortization of deferred losses                             | 122  | 829         | 122                                  | 3,704       |
| Amortization of deferred (gains) losses                                 | 565  | 2,018       | (595)                                | 4,092       |
| (Gains) Losses on termination of interest rate derivatives              | (18)                                       | 2,758       | 1,003                                | 2,758       |
| Total Amortization  | 669  | 5,605       | 530                                  | 10,554      |
| Total charged to interest expense                                       | \$ 4,576                                   | \$ 2,403    | \$ 6,435                             | \$ 7,223    |
| <b>Other Income:</b>  |  |             |                                      |             |
| Mark to market gains (losses) on undesignated interest rate derivatives | \$ 731                                     | \$ 1,072    | \$ 731                               | \$ 1,164    |
| Total charged to other income   | \$ 731                                     | \$ 1,072    | \$ 731                               | \$ 1,164    |

The weighted average interest pay rates of these derivatives were 4.90% at both December 31, 2008 and June 30, 2009.

As of June 30, 2009, we did not have any cash collateral pledged under our interest rate derivatives, nor do we have any existing agreements that require cash collateral postings.

**Management's Use of EBITDA**

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

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

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

**Limitations of EBITDA**

EBITDA has limitations as an analytical tool. It should not be viewed in isolation or as a substitute for GAAP measures of earnings. Material limitations in making the adjustments to our earnings to calculate EBITDA, and using this non-GAAP financial measure as compared to GAAP net income (loss), include:

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

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

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

EBITDA is not an alternative to net income, income from operations or cash flows provided by or used in operations as calculated and presented in accordance with GAAP. You should not rely on EBITDA as a substitute for any such GAAP financial measure. We strongly urge you to review the reconciliation of EBITDA to GAAP net income (loss), along with our consolidated financial statements included elsewhere in this quarterly report. We also strongly urge you to not rely on any single financial measure to evaluate our business. In addition, because EBITDA is not a measure of financial performance under GAAP and is susceptible to varying calculations, the EBITDA measure, as presented in this quarterly report, may differ from, and may not be comparable to, similarly titled measures used by other companies. The table below shows the reconciliation of net income (loss) to EBITDA for the three and six months ended June 30, 2008 and 2009.

|  | <b>Three Months Ended</b>     |             | <b>Six Months Ended</b> |             |
|--|-------------------------------|-------------|-------------------------|-------------|
|  | <b>June 30,</b>               |             | <b>June 30,</b>         |             |
|  | <b>2008</b>                   | <b>2009</b> | <b>2008</b>             | <b>2009</b> |
|  | <b>(Dollars in thousands)</b> |             |                         |             |
| Net income   | \$ 35,341                     | \$ 27,571   | \$ 66,978               | \$ 46,042   |
| Depreciation   | 51,605                        | 51,688      | 99,820                  | 103,249     |
| Amortization of net lease discounts and lease incentives | (2,502)                       | 2,810       | (5,148)                 | 3,927       |
| Interest, net  | 51,319                        | 41,482      | 92,330                  | 84,893      |
| Income tax provision                                     | 1,633                         | 2,049       | 3,347                   | 3,965       |
| EBITDA   | \$ 137,396                    | \$ 125,600  | \$ 257,327              | \$ 242,076  |

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK****Interest Rate Risk**

Interest rate risk is the exposure to loss resulting from changes in the level of interest rates and the spread between different interest rates. These risks are highly sensitive to many factors, including U.S. monetary and tax policies, U.S. and international economic factors and other factors beyond our control. We are exposed to changes in the level of interest rates and to changes in the relationship or spread between interest rates. Our primary interest rate exposures relate to our lease agreements, debt investments, floating rate debt obligations and interest rate derivatives. Rent payments under our aircraft lease agreements typically do not vary during the term of the lease according to changes in interest rates. Similarly, our debt investments are predominately collateralized by fixed rate aircraft leases, and provide for a fixed coupon interest rate. However, our borrowing agreements generally require payments based on a variable interest rate index, such as LIBOR. Therefore, to the extent our borrowing costs are not fixed, increases in interest rates may reduce our net income by increasing the cost of our debt without any corresponding increase in rents or cash flow from our securities.

Changes in interest rates may also impact our net book value as our interest rate derivatives and debt investments are periodically marked-to-market through stockholders' equity. Generally, we are exposed to loss on our fixed pay interest rate derivatives to the extent interest rates decrease below their contractual fixed rate. Also, as interest rates increase, the value of our fixed rate debt investments generally decreases. The magnitude of the decrease is a function of the difference between the coupon rate and the current market rate of interest, the average life of the securities and the face amount of the securities.

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

**Table of Contents****Sensitivity Analysis**

The following discussion about the potential effects of changes in interest rates is based on a sensitivity analysis, which models the effects of hypothetical interest rate shifts on our financial condition and results of operations. We changed our interest rate risk disclosure to an alternative that provides a more meaningful analysis of our interest rate risk. Although we believe a sensitivity analysis provides the most meaningful analysis permitted by the rules and regulations of the SEC, it is constrained by several factors, including the necessity to conduct the analysis based on a single point in time and by the inability to include the extraordinarily complex market reactions that normally would arise from the market shifts modeled. Although the following results of a sensitivity analysis for changes in interest rates may have some limited use as a benchmark, they should not be viewed as a forecast. This forward-looking disclosure also is selective in nature and addresses only the potential minimum contracted rental and interest expense impacts on our financial instruments and our six variable rate leases and, in particular, does not address the mark-to-market impact on our interest rate derivatives. It also does not include a variety of other potential factors that could affect our business as a result of changes in interest rates.

A hypothetical 100-basis point increase/decrease in our variable interest rates would increase/decrease the minimum contracted rentals on our portfolio as of June 30, 2009 by \$1.3 million over the next twelve months. As of June 30, 2009, a hypothetical 100-basis point increase/decrease in our variable interest rate on our borrowings would result in an interest expense increase/decrease of \$0.9 million and \$0.8 million, respectively, net of amounts received from our interest rate derivatives, over the next twelve months.

**Item 4. Controls and Procedures****Management's Evaluation of Disclosure Controls and Procedures**

The term disclosure controls and procedures is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, or the Exchange Act. This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC. An evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer, or CEO, and Chief Financial Officer, or CFO, of the effectiveness of the Company's disclosure controls and procedures as of June 30, 2009. Based on that evaluation, the Company's management, including the CEO and CFO, concluded that the Company's disclosure controls and procedures were effective as of June 30, 2009.

**Changes in Internal Control over Financial Reporting**

There were no changes in the Company's internal control over financial reporting that occurred during the quarter ended June 30, 2009 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents****PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

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

**Item 1A. Risk Factors**

There have been no material changes to the disclosure related to the risk factors described in our Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2008.

**Item 4. Submission of Matters to a Vote of Security Holders**

The annual general meeting of the shareholders of Aircastle Limited was held on May 13, 2009, at which meeting our shareholders voted to (1) elect Wesley R. Edens and Peter V. Ueberroth as Class III directors of the Company, (2) reduce our share premium account by transferring US\$ 1 billion to our contributed surplus account and (3) appoint Ernst & Young LLP as independent registered public accounting firm for the Company for fiscal year 2009 and to authorize the directors of Aircastle Limited, acting by the Audit Committee, to determine the independent registered public accounting firm's fees. The voting results for each proposal submitted to a vote were as listed below.

**Election of Class III Directors:**

|                    | Wesley R.<br>Edens | Peter V.<br>Ueberroth |
|--------------------|--------------------|-----------------------|
| Votes for:         | 41,994,220         | 60,690,786            |
| Votes withheld:    | 19,222,965         | 526,399               |
| Write in nominees: |                    |                       |

The other directors whose terms of office continued after the meeting are: Ronald W. Allen and Douglas A. Hacker as Class I directors; and Joseph P. Adams Jr., John Z. Kukral and Ronald L. Merriman as Class II directors.

**The reduction of our share premium account by transferring US\$ 1 billion to our contributed surplus account:**

|                   |            |
|-------------------|------------|
| Votes for:        | 61,067,246 |
| Votes against:    | 102,154    |
| Votes abstaining: | 47,785     |

**Appointment of Ernst & Young LLP as Independent Public Accounting Firm for Fiscal Year 2009:**

|                   |            |
|-------------------|------------|
| Votes for:        | 60,724,370 |
| Votes against:    | 483,980    |
| Votes abstaining: | 8,835      |



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**Item 6. Exhibits**

| <b>Exhibit No.</b> | <b>Description of Exhibit</b>  |
|--------------------|--|
| 3.1                | Memorandum of Association  |
| 3.2                | Bye-laws   |
| 4.1                | Specimen Share Certificate   |
| 4.2                | Amended and Restated Shareholders Agreement among Aircastle Limited and Fortress Investment Fund III LP, Fortress Investment Fund III (Fund B) LP, Fortress Investment Fund III (Fund C) LP, Fortress Investment Fund III (Fund D) L.P., Fortress Investment Fund III (Fund E) LP, Fortress Investment Fund III (Coinvestment Fund A) LP, Fortress Investment Fund III (Coinvestment Fund B) LP, Fortress Investment Fund III (Coinvestment Fund C) LP, Fortress Investment Fund III (Coinvestment Fund D) L.P., Drawbridge Special Opportunities Fund LP, Drawbridge Special Opportunities Fund Ltd. and Drawbridge Global Macro Master Fund Ltd. |
| 31.1               | Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002   |
| 31.2               | Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002   |
| 32.1               | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| 32.2               | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| 99.1               | Owned Aircraft Portfolio at June 30, 2009  |

Incorporated by reference to the Company's registration statement on Form S-1, filed with the SEC on June 2, 2006, as amended on July 10, 2006, July 25, 2006 and August 2, 2006.

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**SIGNATURE**

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

Dated: August 7, 2009

**AIRCASTLE LIMITED**

(Registrant)

By: /s/ Aaron Dahlke  
Aaron Dahlke  
Chief Accounting Officer and Authorized  
Officer

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