

# IAG's approach to Free Cash Flow and ETS

17 June 2024

# Disclaimer

LEI: 959800TZHQRUSH1ESL13

## Forward-looking statements:

Certain statements included in this document and any related conference call or webcast (including any related Q&A session) are forward-looking. These statements can be identified by the fact that they do not relate only to historical or current facts. By their nature, they involve risk and uncertainties because they relate to events and depend on circumstances that will occur in the future. Actual results could differ materially from those expressed or implied by such forward-looking statements.

Forward-looking statements often use words such as “expects”, “believes”, “may”, “will”, “could”, “should”, “continues”, “intends”, “plans”, “targets”, “predicts”, “estimates”, “envisages” or “anticipates” or other words of similar meaning or their negatives. They include, without limitation, any and all projections relating to the results of operations and financial conditions of International Consolidated Airlines Group, S.A. and its subsidiary undertakings from time to time (the ‘Group’), as well as plans and objectives for future operations, expected future revenues, financing plans, expected expenditure, acquisitions and divestments relating to the Group and discussions of the Group’s business plans and its assumptions, expectations, objectives and resilience with respect to climate scenarios. All forward-looking statements in this document and any related conference call or webcast (including any related Q&A session) are based upon information known to the Group on that date and speak as of that date. Other than in accordance with its legal or regulatory obligations, the Group does not undertake to update or revise any forward-looking statement to reflect any changes in events, conditions or circumstances on which any such statement is based.

Actual results may differ from those expressed or implied in the forward-looking statements in this document and any related conference call or webcast (including any related Q&A session) as a result of any number of known and unknown risks, uncertainties and other factors, including, but not limited to, economic and geo-political, market, regulatory, climate, supply chain or other significant external events, many of which are difficult to predict and are generally beyond the control of the Group, and it is not reasonably possible to itemise each item. Accordingly, readers of this document and participants in any related conference call or webcast (including any related Q&A session) are cautioned against relying on forward-looking statements. Further information on the primary risks of the business and the Group’s risk management process is set out in the Risk management and principal risk factors section in the Annual Report and Accounts 2023; this document is available on [www.iairgroup.com](http://www.iairgroup.com). All forward-looking statements made on or after the date of this document and attributable to IAG are expressly qualified in their entirety by the primary risks set out in that section.

## Alternative Performance Measures:

This document and any related conference call or webcast (including any related Q&A session) contain, in addition to the financial information prepared in accordance with International Financial Reporting Standards (‘IFRS’) and derived from the Group’s financial statements, alternative performance measures (‘APMs’) as defined in the Guidelines on alternative performance measures issued by the European Securities and Markets Authority (ESMA) on 5 October 2015. The performance of the Group is assessed using a number of APMs. These measures are not defined under IFRS, should be considered in addition to IFRS measurements, may differ to definitions given by regulatory bodies relevant to the Group and may differ to similarly titled measures presented by other companies. They are used to measure the outcome of the Group’s strategy based on ‘Unrivalled customer proposition’, ‘Value accretive and sustainable growth’ and ‘Efficiency and innovation’.

For definitions and explanations of alternative performance measures, refer to the Alternative performance measures section in the [IAG Annual Report and Accounts 2023 \(iairgroup.com\)](http://www.iairgroup.com) and the Interim Management Report for the three months to 31 March 2024 ([IAG Q1 2024 Results \(iairgroup.com\)](http://www.iairgroup.com)). These documents are available on [www.iairgroup.com](http://www.iairgroup.com)

# Contents

1. Free Cash Flow - definition, calculation and approach
2. IAG's approach to IFRS 16 - on adoption from 1 January 2019 and ongoing
3. ETS in IAG's accounts

# Free cash flow – IAG calculation

## Alternative performance measures

### e Free cash flow <sup>(KPI)</sup>

Free cash flow represents the cash generated by the businesses and is defined as the net cash flows from operating activities taken from the Cash flow statement, less the cash flows associated with the acquisition of property, plant and equipment and intangible assets reported in net cash flows from investing activities from the Cash flow statement. The Group believes that this measure is useful to the users of the financial statements in understanding the cash generating ability of the Group to support operations and maintain its capital assets.

€ million	2023	2022
<b>Net cash flows from operating activities</b>	<b>4,864</b>	4,854
Acquisition of property, plant and equipment and intangible assets	<b>(3,544)</b>	(3,875)
<b>Free cash flow</b>	<b>1,320</b>	979

*IAG 2023 Annual report and accounts  
Alternative performance measures, page 292*

# Free cash flow – IAG’s principles

- Calculate the cash that the business generates which is ‘free’ for uses such as:
  - shareholder returns
  - debt reduction
  - other corporate initiatives
- Include all relevant cashflows (i.e. operating and capital expenditure)
- Include cashflows only once
- Be agnostic as to future financing decisions
- Make the measure simple and transparent to calculate from IAG’s public releases
- Show the calculation of the measure as an Alternative Performance Measure (APM)

## Choice of aircraft financing results in different impacts in the financial statements

	Owned	Finance Lease* (inc. JOLCOs)	Operating Lease (sale and leaseback)	Direct Lease
<b>Nature</b>	Airline specifies and purchases aircraft – pays for cash with no refinancing	Airline specifies and purchases aircraft; negotiates financing separately and executes after delivery	Airline specifies and purchases aircraft; negotiates financing separately and executes after delivery	Lessor purchases aircraft from manufacturer; airline negotiates financing with lessor
<b>Capex</b>	☑	☑	☑	☒
<b>Balance sheet asset value</b>	Cost less depreciation	Cost less depreciation	Right of use asset less depreciation	Right of use asset less depreciation
<b>P&amp;L charge</b>	Depreciation	Depreciation and interest	Depreciation and interest	Depreciation and interest
<b>Cashflow lines</b>	Depreciation  Capex	Depreciation Interest paid Capex Proceeds from borrowings Repayment of asset financed liabilities	Depreciation Interest paid Capex Sale of PPE Repayment of lease liabilities	Depreciation Interest paid  Repayment of lease liabilities

\* Includes Japanese Operating Lease with Call Option (JOLCO) structures, a common form of finance lease used in the aviation sector.

# IAG uses Gross Capex; we do not double-count leased aircraft

€ million	Note	Year to 31 December	
		2023	2022 <sup>1</sup>
<b>Cash flows from operating activities</b>			
Operating profit		3,507	1,278
Depreciation, amortisation and impairment	6	2,063	2,070
Net gain on disposal of property, plant and equipment		(2)	(22)
Employer contributions to pension schemes		(48)	(22)
Pension scheme service costs	34	18	17
Increase in provisions	35	237	463
Unrealised currency differences		51	19
Other movements	35	111	76
Interest paid		(1,005)	(817)
Interest received		365	42
Tax paid		(291)	(134)
<b>Net cash flows from operating activities before movements in working capital</b>		<b>5,006</b>	<b>2,970</b>
Increase in trade receivables		(272)	(660)
Increase in inventories		(140)	(21)
Increase in other receivables and current assets		(388)	(233)
Increase in trade payables		258	886
Increase in deferred revenue		212	1,236
Increase in other payables and current liabilities		188	676
<b>Net movement in working capital</b>		<b>(142)</b>	<b>1,884</b>
<b>Net cash flows from operating activities</b>		<b>4,864</b>	<b>4,854</b>
<b>Cash flows from investing activities</b>			
Acquisition of property, plant and equipment and intangible assets	35	(3,544)	(3,875)

**Free Cash Flow (FCF)**

We include all aircraft capital expenditure, irrespective of how aircraft are subsequently financed, i.e.:

- 1) Owned outright
- 2) Finance leases
- 3) Operating leases

We use GROSS capex and so do not need to deduct the principal element of operating lease payments – if we did, we would be double-counting the aircraft cost.

This works for IAG, as we have very few aircraft that are leased directly from lessors – the substantial majority of operating leased aircraft are ordered by IAG from manufacturers under IAG deals, paid for from IAG's cash and are then subsequently subject to sale and leaseback transactions as part of our financing strategy.

# Other cashflow items: Lease liabilities include more than just operating leases

## Cash flows from investing activities

Acquisition of property, plant and equipment and intangible assets	35	(3,544)	(3,875)
Sale of property, plant and equipment and intangible assets		1,080	837
Proceeds from sale of investments		11	-
Increase in other current interest-bearing deposits		(985)	(351)
Payment to Globalia for convertible loan		-	(100)
Other investing movements		15	26

## Net cash flows from investing activities

## Cash flows from financing activities

Proceeds from borrowings	35	1,001	1,436
Repayment of borrowings	35	(4,268)	(1,050)
Repayment of lease liabilities	35	(1,731)	(1,455)
Settlement of derivative financial instruments	35	(119)	1,036
Acquisition of treasury shares		(77)	(23)
<b>Net cash flows from financing activities</b>		<b>(5,194)</b>	<b>(56)</b>

Note	Year to 31 December	
	2023	2022 <sup>1</sup>
	(3,544)	(3,875)
	1,080	837
	11	-
	(985)	(351)
	-	(100)
	15	26
	(3,423)	(3,463)
	1,001	1,436
	(4,268)	(1,050)
	(1,731)	(1,455)
	(119)	1,036
	(77)	(23)
	(5,194)	(56)

Proceeds from sale and leaseback transactions and other minor disposals

Movement between cash invested <3 months and >3 months (up to 12 months)

Payment of bank debt, including COVID-19 related UKEF, ICO and ISIF backed, as well as principal element of finance leases from 1 January 2019 onwards

Payment of principal element of both finance leases in place before 1 January 2019 (due to IFRS 16 adoption method) and operating leases

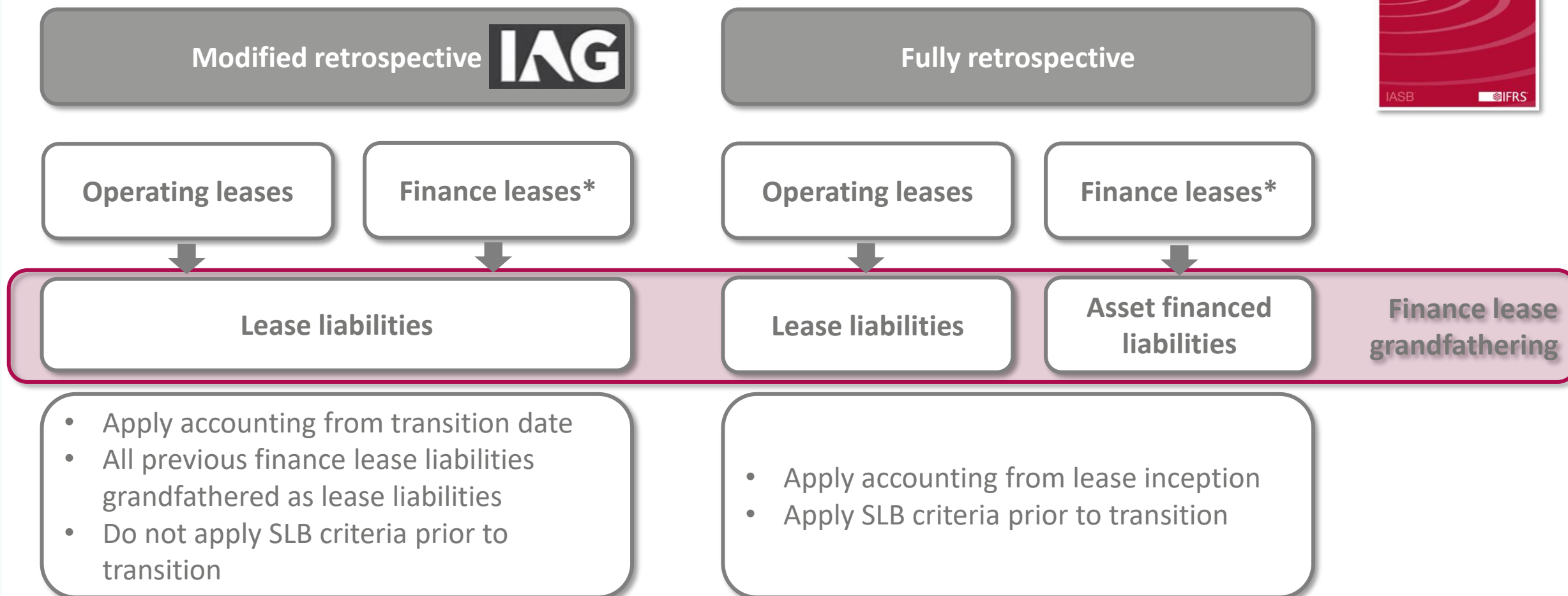
Substantially all new aircraft debt (finance leases)

FX hedging related to debt repayments

Typically only management incentive related (2023: 15m shares); also includes in 2023 27m shares as 50% of Air Europa acquisition requirement



# Application of IFRS 16 on transition (1 January 2019): impacted both operating leases and finance leases



\* Includes Japanese Operating Lease with Call Option (JOLCO) structures, a common form of finance lease used in the aviation sector.

# Sale and lease-back criteria for accounting

## Sale and leaseback transactions

Assess whether a “sale” occurred under IFRS 15 *Revenue from contracts with customers*

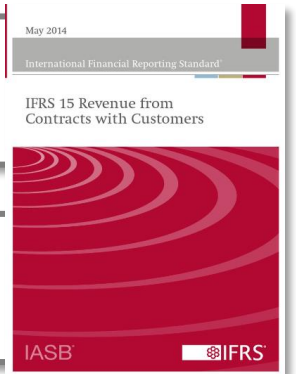
Does the lease contain a purchase option, irrespective of intent to exercise?

Yes – do not apply IFRS 16

No – apply IFRS 16

Recognise Asset financed liability and do not de-recognise asset

Recognise lease liability and Right of use asset



# Accounting for aircraft financing – with pre/post 1 Jan 2019 split of finance leases

	Owned	Finance Lease* (inc. JOLCOs) Post 1 Jan 2019	Finance Lease* (inc. JOLCOs) Pre 1 Jan 2019	Operating Lease (sale and leaseback)	Direct Lease
<b>Nature</b>	Airline specifies and purchases aircraft – pays for cash with no refinancing	Airline specifies and purchases aircraft; negotiates financing separately and executes after delivery	Airline specifies and purchases aircraft; negotiates financing separately and executes after delivery	Airline specifies and purchases aircraft; negotiates financing separately and executes after delivery	Lessor purchases aircraft from manufacturer; airline negotiates financing with lessor
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# Differences between Asset financed liabilities and lease liabilities

	Asset financed liability	Lease liabilities	Comments
Debt recognition	Recognised at amount received from lessor	Recognised at the value of future lease payments	Value of debt will differ between categories
Asset recognition	Owned asset retained	Right of use (ROU) asset matches lease liability recognised	Asset values will differ
Depreciation	Depreciated over 23-29 years	Depreciated over lease term	Annual depreciation will usually be higher for ROU asset
Interest	Rate that discounts all lease payments to proceeds received	Rate that discounts all lease payments and residual value to inception fair value	Rates will differ – giving rise to different P&L charges

# Leases in the Income/Cash flow statements

## CONSOLIDATED INCOME STATEMENT

€ million	Note	Year to 31 December	
		2023	2022 <sup>1</sup>
Passenger revenue		25,810	19,458
Cargo revenue		1,156	1,615
Other revenue	5	2,487	1,993
<b>Total revenue</b>	5	<b>29,453</b>	23,066
Employee costs	8	5,423	4,647
Fuel, oil costs and emissions charges		7,557	6,120
Handling, catering and other operating costs		3,849	2,971
Landing fees and en-route charges		2,308	1,890
Engineering and other aircraft costs		2,509	2,101
Property, IT and other costs	6	1,058	950
Selling costs		1,155	920
Depreciation, amortisation and impairment	6	2,063	2,070
Net gain on sale of property, plant and equipment <sup>1</sup>		(2)	(22)
Currency differences		26	141
Total expenditure on operations		25,946	21,788
<b>Operating profit</b>		<b>3,507</b>	1,278
Finance costs	9	(1,113)	(1,017)
Finance income	9	386	52
Net change in fair value of financial instruments	9	(11)	81
Net financing credit relating to pensions	9	103	26
Net currency retranslation credits/(charges)		176	(115)
Other non-operating credits <sup>1</sup>	9	8	110
Total net non-operating costs		(451)	(863)
<b>Profit before tax</b>		<b>3,056</b>	415
Tax	10	(401)	16
<b>Profit after tax for the year</b>		<b>2,655</b>	431

All leases, either operating or finance, are reflected in the Income statement through Depreciation and Finance costs.

Differs to US GAAP for operating leases.

All leases, either operating or finance, are reflected in the Cash flow statement through Interest paid and either Repayment of borrowings (general debt and finance leases from 1 Jan 2019 onwards) or Lease liabilities (operating leases and finance leases in place before 1 Jan 2019)

## CONSOLIDATED CASH FLOW STATEMENT (extract)

€ million	Note	Year to 31 December	
		2023	2022 <sup>1</sup>
<b>Cash flows from operating activities</b>			
Operating profit		3,507	1,278
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Increase in trade payables		258	886
Increase in deferred revenue		212	1,236
Increase in other payables and current liabilities		188	676
<b>Net movement in working capital</b>		<b>(142)</b>	1,884
<b>Net cash flows from operating activities</b>		<b>4,864</b>	4,854
<b>Cash flows from financing activities</b>			
Proceeds from borrowings	35	1,001	1,436
Repayment of borrowings	35	(4,268)	(1,050)
Repayment of lease liabilities	35	(1,731)	(1,455)
Settlement of derivative financial instruments	35	(119)	1,036
Acquisition of treasury shares		(77)	(23)
<b>Net cash flows from financing activities</b>		<b>(5,194)</b>	(56)

# In 2023 'Repayment of lease liabilities' was c50% finance leases dating from pre 1 January 2019

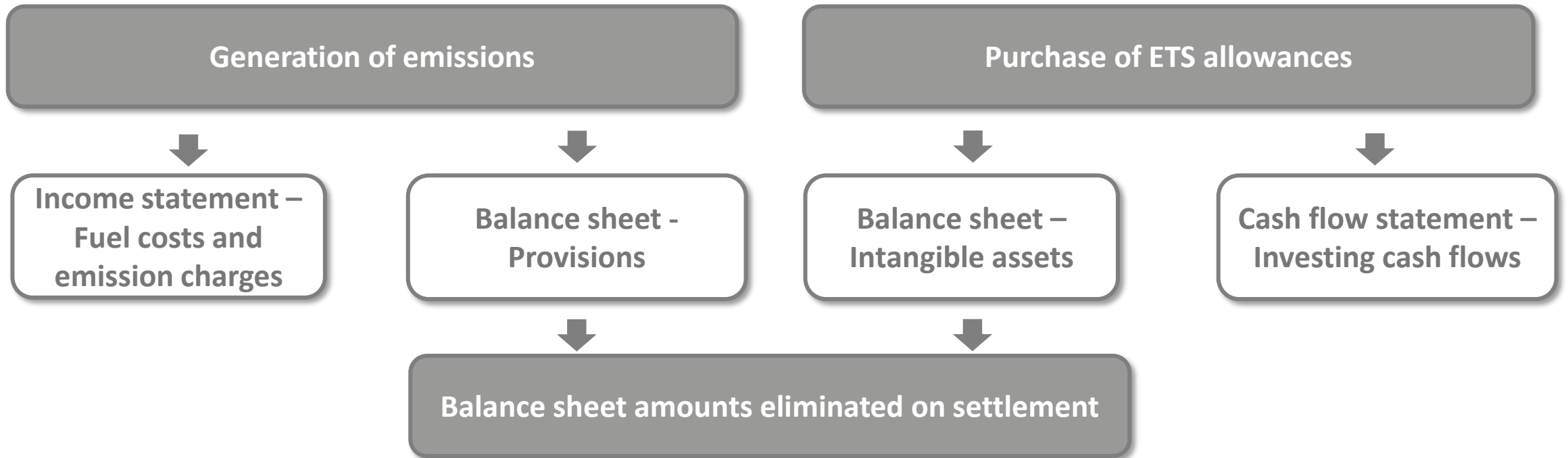
## Cash flows from financing activities

	Note	Year to 31 December	
		2023	2022 <sup>1</sup>
Proceeds from borrowings	35	1,001	1,436
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The breakdown of this item was split in 2023 approximately 50:50 between operating leases and finance leases dating from before 1 January 2019

- The item 'Repayment of lease liabilities' in 2023 included those finance leases still in place that were entered into before 1 January 2019. These payments will reduce over time as leases mature, with approximately 7 years still to run, and the reduction related to the profile of maturity payments on leases, rather than linear.
- We plan and measure internally without making assumptions on specific proportions of sale and leaseback transactions, as we prefer to separate financing decisions from investment decisions and make financing decisions nearer to the point of delivery of the aircraft.
- However, we are aware some people use Net capex less operating lease debt principal repayments. The Gross capex and sale of PPE/intangibles is given on the face of the Cash flow statement (i.e. to calculate Net capex). The information above would facilitate an estimate of the operating lease principal repayments (i.e. c50% of €1,731m in 2023).
- We are intending to include further disclosure in the 2024 Annual report and accounts to facilitate splitting the item Repayment of lease liabilities between: (i) operating leases and (ii) finance leases dating from before 1 January 2019.

# Accounting for ETS allowances



**P&L and Cash Flow Statement amounts will not match**

(P&L is on a provisions basis – what was incurred in the year; Cash Flow is based on the ETS allowances the Group purchased in the year)

# ETS cash flows in 2023

€ million	Note	Year to 31 December	
		2023	2022 <sup>1</sup>
<b>Cash flows from operating activities</b>			
Operating profit		3,507	1,278
Depreciation, amortisation and impairment	6	2,063	2,070
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<b>Cash flows from investing activities</b>			
Acquisition of property, plant and equipment and intangible assets	35	(3,544)	(3,875)

Operating expenditures include a provision for ETS costs incurred in the year, within 'Fuel, oil costs and emissions charges'

In the Cash Flow Statement, this provision is reversed out through the provisions movement line (as non-cash).

The actual cash spend on ETS in a given year is included within capex. This represents all the ETS allowances the Group chooses to purchase in that year, which will typically be for the following years' ETS requirements.



# ETS accounting in 2023

## 27 Provisions

€ million	Restoration and handback provisions	Restructuring provisions	Employee leaving indemnities and other employee related provisions	Legal claims and contractual disputes provisions	ETS provisions	Other provisions	Total
Net book value 1 January 2023	2,400	194	673	89	132	60	3,548
Provisions recorded during the year	520	1	53	15	238	32	859
Reclassifications	4	-	-	(1)	-	(6)	(3)
Utilised during the year	(338)	(82)	(35)	(9)	-	(32)	(496)
Extinguished during the year	-	-	-	-	(98)	-	(98)
Release of unused amounts	(68)	(21)	(2)	(15)	(26)	(1)	(133)
Unwinding of discount	78	2	23	-	-	-	103
Remeasurements	4	-	24	-	-	-	28
Exchange differences	(71)	-	(1)	3	1	-	(68)
<b>Net book value 31 December 2023</b>	<b>2,529</b>	<b>94</b>	<b>735</b>	<b>82</b>	<b>247</b>	<b>53</b>	<b>3,740</b>

Provision recognised of €238 million with charge to the **Income statement** within Fuel, oil costs and emission charges

## 17 Intangible assets and impairment review

### a Intangible assets

€ million	Goodwill	Brand	Customer loyalty programmes	Landing rights <sup>1</sup>	Software	ETS assets	Other	Total
<b>Cost</b>								
Balance at 1 January 2022	596	451	253	1,605	1,674	62	87	4,728
Additions	-	-	-	14	218	360	1	593
Disposals	-	-	-	(6)	(52)	(9)	-	(67)
Exchange movements	(1)	-	-	(25)	(34)	(6)	-	(66)
Balance at 31 December 2022	595	451	253	1,588	1,806	407	88	5,188
Additions	-	-	-	-	365	264	1	630
Disposals	-	-	-	(6)	(49)	(96)	-	(151)
Reclassifications	-	-	-	-	23	-	(15)	8
Exchange movements	1	-	-	11	18	2	-	32
<b>31 December 2023</b>	<b>596</b>	<b>451</b>	<b>253</b>	<b>1,593</b>	<b>2,163</b>	<b>577</b>	<b>74</b>	<b>5,707</b>

## 35 Supplemental cash flow information

### d Details of acquisition of property, plant and equipment and intangible assets within Net cash flows from investing activities

€ million	2023	2022
Purchase of property, plant and equipment - fleet	2,715	3,146
Purchase of property, plant and equipment - other	193	132
Purchase of intangible assets - ETS allowances	264	360
Purchase of intangible assets - other	372	237
	<b>3,544</b>	<b>3,875</b>

All Investing cash flows of €264 million reflected as Intangible assets

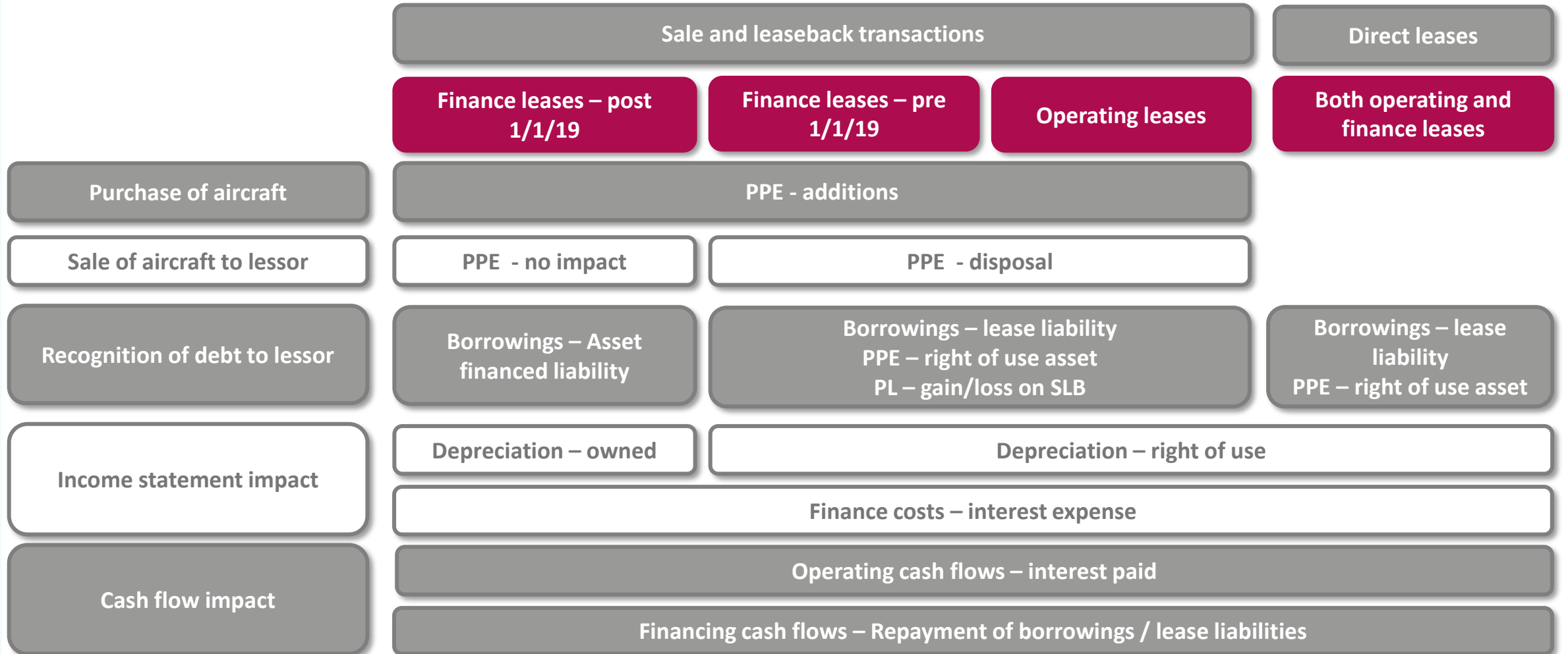
A reminder from our Q4-2023 results presentation

# Strong free cash flow of €1.3bn and positive drivers for 2024

	€m	2023	2024
<b>Operating profit</b>	<b>3,507</b>	ASK grew 22.6% vly	ASK growth around 7% in 2024 and 4-5% over three years 2024-2026
Depreciation	2,063		Increases as investment increases
Working capital	(142)	Impacted by €0.2bn delayed receivables payments	Unwind of 2023 collections timing; increase in revenue
Pension	(30)	No contributions made to NAPS and APS	No additional contributions anticipated
Provisions	237	ETS, net of restructuring and maintenance	ETS increases as credits are phased out
Interest paid	(1,005)	Repayment of expensive debt with average cost of borrowing of c.9%	Lower, to reflect debt repayments in 2023 (c.€200m in Q4 2023)
Interest received	365	Average interest rate of 3.7%	Average rate expected to stay broadly the same
Tax paid	(291)	Cash tax rate of c.10% of profits before tax	Expected cash tax rate continues to benefit from available losses
Other	160	FX and other items	
<b>Net cash from Op activities</b>	<b>4,864</b>		
Gross capex	(3,544)	Slightly lower than planned	€3.7bn in 2024 and average of €4.5bn over 3 years (2024 – 2026)
<b>Free cash flow</b>	<b>1,320</b>		

## Appendix

# Accounting for leases



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