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| <p>In the published version of this decision, some information has been omitted as privileged and confidential. The omissions are shown thus [...]. The omissions have been made pursuant to Article 22 of the State Aid Act and statutory rules concerning non-disclosure of information covered by professional secrecy.</p> | <p style="text-align: center;">PUBLIC VERSION</p> <p>This document is made available for information purposes only.</p> |
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The Republic of Serbia
STATE AID COMMISSION
Number: 142/2/2013-38
Belgrade, 21 February 2014

In accordance with Article 9, points 2) and 3) and Article 16 paragraph 1 of the State Aid Act (“Official Gazette of the RS”, No. 51/09) and Article 192 of the General Administrative Procedure Act (“Official Gazette of the FRY”, Nos. 33/97 and 31/01 and “Official Gazette of the RS”, No. 30/10) in an ex post control proceedings, initiated based on our own information,

The State Aid Commission, at its 66th session held on 21 February 2014, hereby enacts the following

D E C I S I O N

1. State aid for the restructuring of the Joint Stock Company for Air Traffic “Air Serbia”, Belgrade, 16A, Bulevar Umetnosti street is hereby approved.
2. The Office of the First Deputy Prime Minister of the Government (as the applicant for state aid approval) shall regularly provide the State Aid Commission with annual reports on the progress of implementing the restructuring plan, until completion of the restructuring process in the Joint Stock Company for Air Traffic “Air Serbia”, Belgrade, as well as inform the State Aid Commission in writing on completion of the restructuring process, as soon as they are informed thereof by the company.
3. This resolution shall be published on the website of the State Aid Commission.

R e a s o n i n g

I. Initiation and Course of State Aid Control Proceedings

By the Letter No: 420-01-2/13-5 dated 14 October 2013, the Ministry of Economy provided the State Aid Commission (hereinafter: the Commission) with the Proposal of the Conclusion Approving the Issuance

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of a Guarantee by the Development Fund of the Republic of Serbia, per request of Joint Stock Company for Air Traffic "Air Serbia" a.d. Beograd, in favor of ETIHAD AIRWAYS P.J.S.C. (hereinafter: the Conclusion Proposal), for the purpose of its review from the aspect of state aid regulations.

From the rationale of the Conclusion Proposal, the Commission established that this is one of the measures foreseen by the agreements entered into on 1 August 2013 by and between the Government of the Republic of Serbia, the company Etihad Airways from Abu Dhabi, United Arab Emirates (hereinafter: Etihad), and the Joint Stock Company for Air Traffic "JAT Airways" a.d. Beograd Jat Airways (hereinafter: Jat Airways).

Having obtained information which indicates that this might be considered state aid which was not applied for, in accordance with the meaning of Article 11, paragraph 1 of the State Aid Act ("Official Gazette of the RS", no. 51/09 – hereinafter: the Act), by its Conclusion No: 142/2013-38 dated 9 December 2013 the Commission initiated ex post control proceedings of the legality of state aid granted to the aid recipient Air Serbia, and instructed the Office of the First Deputy Prime Minister of the Government, as the signatory of the Agreements to, immediately upon receipt of this conclusion, file a state aid application.

The Office of the First Deputy Prime Minister of the Government (hereinafter: the Applicant), acting in accordance with the Commission's instructions, by its Letter 04 No: 023-00-11/2013 dated 12 December 2013, provided the General State Aid Application Form and the Special State Aid Application Form for Reporting State Aid for Restructuring of Firms in Difficulty, in accordance with Article 3 paragraph 2 of the Regulation on the Manner and Procedure for Reporting of State Aid ("Official Gazette of the RS", No. 51/09).

In the further course of ex post control proceedings, the Applicant addressed the Commission with a request for an opinion on whether the Act applies to decisions on granting of state aid which were adopted before this act started to be applied, that is, whether it was necessary to notify to the Commission any state aid which was granted prior to the act started to be applied.

The Commission stated in its response that full application of the Act was not possible prior to the establishment of the Commission, as well as prior to the enactment of rules specified in the Regulation on the Manner and Procedure for Reporting of State Aid and in the Regulation on the Regulation for Granting of State Aid ("Official Gazette of the RS", Nos. 13/10, 100/11, 91/12, 37/13, and 97/13 – hereinafter: the Regulation), thus the full application of the Act started on 20 March 2010. Therefore, in accordance with this response, state aid which was granted prior to the start of the Act's application, i.e. prior to 20 March 2010 needs not be reported to the Commission, i.e. such aid is not subject to state aid rules and the Commission shall not decide on its legality.

In the further course of proceedings, the Applicant delivered the following to the Commission, for the purpose of deciding on its legality:

- Rescue and Restructuring Plan for the company Air Serbia and all annexes thereto (hereinafter: the Restructuring Plan),

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- Excerpt from the Company Registry maintained by the Business Registry Agency,
- Report of the Financial Affairs Directorate of the company Air Serbia on most important obligations of the company as of 31 October 2013,
- Overview of due and unsettled obligations of the company Air Serbia as of 31 October 2013, with a division of obligations dating prior to 31 December 2009 and those dating after 1 January 2010,
- Evaluation of real estate of Air Serbia, which are proposed to be offered for sale;
- Proof of achieved savings with regard to procurement of new aircraft.

The Applicant stated that all provided documents shall be considered a business secret, in accordance with the meaning of Arts. 1 and 2 of the Business Secret Protection Act ("Official Gazette of the RS", No. 72/2011).

Details Regarding the State Aid Recipient

From the excerpt from the Business Registry Agency the following business information regarding the state aid recipient have been established:

Name: Air SERBIA

Business Name: Joint Stock Company for Air Traffic Air SERBIA, Beograd

Status: Active company

Registration number: 07044275

Legal form: Joint stock company

Seat: Municipality: New Belgrade / Town: Belgrade – New Belgrade / Street and no: 16A, Bulevar Umetnosti

Date of incorporation: 29 February 1992

Tax ID no: 100001765

Date of registration: 25 February 2005

Activity code: 5110

Activity name: Passenger Air Transport

II Restructuring Plan

From the review of due and unsettled obligations of Air Serbia, it is undisputable that Air Serbia is a firm in difficulty and that it is not capable through its own funds, the funds of its owners/shareholders or of its

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creditors, or through other sources at the market, to prevent losses which would, without the state's intervention, jeopardize its survival in the short or medium term, in accordance with Article 2, paragraph 1, point 5) of the Regulation.

Having this in mind, it would only be possible to provide rescue and restructuring state aid to a firm in difficulty, so the Applicant submitted to the Commission the Restructuring Plan.

Together with the Restructuring Plan, as an integral part thereof, respective addendums have also been submitted as detailed in point 1 of the Reasoning to this decision.

1. Description of the Restructuring Plan

Introduction

For the purposes of the air carrier's restructuring, the Government of the Republic of Serbia accepted to sell 49% of shares to Etihad, so that Etihad would use its experience and provide expert assistance to Air Serbia, [...].

The company Jat Airways changed its name to Air Serbia in October 2013, in accordance with the rebranding strategy, so the Restructuring Plan relates to Air Serbia (including the period prior to the rebranding).

Air Serbia is a Firm in Difficulty

The Restructuring Plan specifies the reasons for difficulties in Air Serbia's operations in the preceding period, which can be divided into two basic groups: those internal in nature and external in nature, on which Air Serbia could not have influenced.

A larger number of internal factors had an adverse effect to Air Serbia's operations during the last several years:

- Outdated fleet (average aircraft age is 26 years), which does not fulfill the business needs and causes high operational costs and frequent technical difficulties. Air Serbia's fleet attempted, with significant efforts, to operate a non-profitable network of routes, which was not setup so as to maximize traffic or to attract transfer passengers to travel via Belgrade.
- Historical obligations prevented the operational restructuring of the business.
- Inadequate corporate governance of the company and lack of expertise resulted in low productivity, inadequately used human resources, and inadequately used fleet.
- Recent adverse market conditions – lack of economic growth in the Republic of Serbia, devaluation of the Serbian dinar (RSD) against the US dollar (USD), entry of low-cost carriers into the market – resulted in additional pressure on the number of passengers and revenues.

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Having in mind the above, state aid for restructuring is necessary, in order to avoid the termination of the commercial entity and significant social hardship which the Serbian economy would consequently endure.

Termination of the Company Air Serbia Would Result in Significant Social Hardship

Termination of the company Air Serbia would result in significant economic and social losses:

- Unemployment in the Republic of Serbia is more than two times higher than the European Union average. Termination of Air Serbia would worsen this situation. The report made by the Oxford Economics Institute estimates that the economic contribution of the company Air Serbia to the entire economy of the Republic of Serbia exceeds USD 700 million per annum (according to prices in 2014), so its direct, as well as indirect effects on the rate of unemployment is reflected in the creation of approximately 21.000 new jobs in the Republic of Serbia.
- The indirect and long-term damages which the economy of the Republic of Serbia would suffer due to loss of its national air carrier would be incomparably higher. This would reduce the trust by international investors to invest further into the Republic of Serbia, which would in turn create a direct negative risk for the businesses in the export and tourism sectors, and have a negative effect on the business of national airports.
- The position of the Republic of Serbia within the region and within Europe would thereby be endangered, which would also undermine the integration and connectivity of the Republic of Serbia with the EU Single Market.

Etihad Has Agreed to Purchase a 49% Stake in Air Serbia

The participation of private capital and hiring of experts is of essential importance for restoring long term viability of Air Serbia. Etihad has a vast experience in successfully implementing restructuring projects. The readiness of Etihad to accept a significant financial risk, as well as a reputational risk, shows the faith of this company in the future sustainability and competitiveness of Air Serbia, as well as the experience of the new management in the implementation of the restructuring.

Etihad shall, as part of the proposed transaction, provide expert assistance to Air Serbia, [...]. The Government of the Republic of Serbia and Etihad agreed to jointly finance the restructuring process of Air Serbia.

It is expected that the partnership of Air Serbia with Etihad shall result in a number of benefits:

- Corporate governance – Etihad will bring strong private sector governance in order to increase the efficiency of the business and decision making in the national air carrier.
- Expertise and experience – Etihad will implement its experience gained in the civil aviation sector in order to optimize the fleet utilization plan and network route of Air Serbia's air traffic.

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Other than this, a number of operational functions in Air Serbia can be centralized in order to reduce costs and increase efficiency.

- Synergy effects in procurement – Etihad shall provide better negotiating leverage in negotiations with all major suppliers, at the hub and ancillary airports, and consolidate the procurement system on a global level, in order to secure quantity discounts.
- Access to a global network – Air Serbia will become a member of the global alliance of air carriers, so as to ensure better connectivity on the international and regional markets, which will result in increased air traffic through Belgrade.

The Government of the Republic of Serbia and Etihad Agreed to Share the Burden and Risk of Air Serbia's Restructuring Measures

Historic measures up to the first quarter of 2014:

The historical debt of Air Serbia, estimated at USD [...] (as of December 2012), must be eliminated in order to ensure operational restructuring of the company.

Privatization in accordance with market conditions 1 August 2013:

Amongst the few valuable assets of Air Serbia are the landing slots on a large number of international airports. Their value could not have exceeded USD [...].

Restructuring during the transaction period, August 2013 – 1st quarter 2014:

During the transactional period, a number of restructuring measures have been undertaken – in August 2013 a redundancy program for employees was initiated and over [...] of voluntary redundancy procedures have been completed.

The total cost of restructuring measures between 1 August 2013 and 1st quarter 2014 amounts to cca USD [...]. Part of these funds shall be used to finance the future business of Air Serbia. This includes the state guarantee for a loan to be provided by Etihad in the amount of USD [...]. This guarantee shall continue to be in force after the transaction period.

Restructuring in the post-transactional period 1st quarter 2014 – December 2016:

Total costs of restructuring after 1st quarter 2014 are estimated at USD [...] (not including the state guarantee for the loan, which was included for the previous period).

Air Serbia Plans to Focus on Six Areas in Order to Restore Viability and Competitiveness

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Planning of air traffic routes – [...]

A consultant company [...] developed a business model in order to define the optimal flight schedule and fleet size.

- Reduction of number of employees – Air Serbia made an initial analysis of the number of employees and of productivity in July 2013. Based on the analysis, an optimal number of employees was estimated necessary for the realization of the planned productivity levels, defined on the basis of parameters in the aviation sector and consolidation of the main business units within Etihad. Based on the initial estimates, staff costs are expected to decrease by over USD [...] per month.
- Renewal of the fleet – In the mid-term period, Air Serbia plans to renew its fleet with 10 aircraft A319/320 [...] that are expected to be approximately 18% more fuel-efficient than the existing fleet. [...] Additionally, a short-term pilot training plan was made for the Airbus fleet aircraft.
- New governance structure – A new governance structure will ensure the establishment of adequate internal controls and processes in the restructured business. The new governance structure shall be supported by management made up of experienced experts – focused on the implementation of the business plan and on initiatives which have for their goal the implementation of synergy effects on the business.
- Synergy effects in the procurement domain – Air Serbia is planning to use Etihad's experience in negotiations with major suppliers. For example, [...]. Additionally, Etihad's experience can strengthen the negotiating position of Air Serbia in negotiations with aircraft manufacturers. It is expected that the full synergy effects in procurement will be achieved by 2016.
- Other measures – Air Serbia plans to adopt a commercial strategy and a rebranding strategy in order to improve sales. This entails the change of name from JAT Airways to Air Serbia, which was already done, creating a new website for on-line sales, improvements to ticket sales in Belgrade, improved offer to clients in business class and an improved marketing approach.

Restructuring Plan of Company Air Serbia Aims to Return to Long Term Viability within Three Years According to the Basic Scenario

The model based on information provided by Air Serbia and developed by PricewaterhouseCoopers LLP of UK (hereinafter: PwC), was made in order to evaluate whether the Restructuring Plan will ensure restoring long term viability of Air Serbia. The model was developed based on the data on revenues and the cost drivers provided by Etihad and Air Serbia – i.e. fuel costs, speed of fuel combustion, revenue per passenger, load factors, maintenance and navigation costs, employee costs.

The model includes financial forecasts for the following five years. The forecasts from financial year 2014 (FY14) to financial year 2016 (FY16) were made based on data from individual air traffic routes on a monthly level. The forecasts of inputs and outputs for FY17 and FY18 were made on an annual level, and the model was made only on the group level (not on the level of air traffic routes).

Based on the model of the baseline scenario, it is expected that Air Serbia will return to long term viability within three years.

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The subsidies for business financing are not needed after 2016, when the business is expected to reach profitability. This is reflected in the financial forecasts which rely on such subsidies.

Air Serbia made a stress-test of the Restructuring Plan under two possible downside scenarios: unexpected and sudden increase of fuel prices and increased competition by low-cost air carriers on the Air Serbia most sensitive routes.

Based on the model it is expected that Air Serbia will be capable to absorb losses which would arise in the mentioned scenarios and return to long term viability without additional state aid. For example, it is expected that over the next five years, Air Serbia will secure sufficient funds to absorb an increase in fuel prices of [...] % without requesting additional state aid. The management developed strategies for alleviating the risk of possible negative outcomes.

Considering that some of the restructuring measures have already been implemented (i.e. reduction of the number of employees) and that the remaining measures will be implemented in the first half of the restructuring period, it is possible that Air Serbia will return to long term viability even before the deadlines from the baseline scenario.

According to the Restructuring Plan, the Restructured Airline Is Unlikely To Be in a Position To Distort Competition

It is not expected that state aid granted in the restructuring of Air Serbia will have adverse effect on the air traffic market in the European Union due to its [Air Serbia's] relatively small position in the market.

Prior to the restructuring, Air Serbia had less than [...] of the EU market according to the number of passengers and seat capacity. After the restructuring the market share will most likely be significantly below [...].

After the restructuring, Air Serbia's seat capacity is expected to be reduced by approximately [...], as stated in the Restructuring Plan.

Simultaneously, the transaction between Etihad and Air Serbia was approved by the competition authorities in the Republic of Montenegro, the Republic of Germany, and the Republic of Serbia.

2. An Overview of the Air Serbia Business

A large number of air carriers from Europe, Africa, and the Middle East operate in the aviation sector of the Republic of Serbia.

From 2005, this sector has been steadily increasing in capacity at a rate of cca 3% per year. The implementation of the Open Sky policy in the Serbian market attracted new air carriers, and low-cost

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carriers and charter airlines showing increasing interest in the Nikola Tesla Airport (Belgrade Airport) over the past three years. Currently, over 20 air carriers are flying into and out of the Republic of Serbia.

As of July 2013, approximately [...] of capacity relates to flights from Western Europe, or to Western Europe; [...] - to Eastern Europe; [...] to the Middle East; and [...] to Northern Africa.

With an outdated fleet, limited number of air traffic routes, and limited offer of destinations, Air Serbia is, according to EU standards, a very small commercial entity (it takes up [...] of the EU market in terms of seat capacity and passengers carried in 2012). As of the middle of 2013, Air Serbia flew to [...] destinations in the summer and to [...] destinations in the winter season. These were mostly European destinations.

3. Air Serbia – A Firm in Difficulty

Air Serbia is a firm in difficulty because:

- It is technically insolvent;
- It has lost more than one quarter of its registered capital over the past year;
- It is unable to meet its short-term liabilities due to cash constraints.

Current Financial Distress

Air Serbia has a significant negative equity in the amount of USD [...] with a tendency for further negative growth.

Operations are burdened with a total financial debt amounting to cca [...] at the end of 2012.

Air Serbia has significant debts towards its creditors (mostly companies providing ground handling services, navigation, and aircraft maintenance).

As of May 2013, cash funds amounted to cca USD [...].

Causes of Financial Distress

The Restructuring Plan specifies several interrelated factors which caused significant financial distress of Air Serbia:

- Outdated fleet which does not fulfill the requirements of performing the main activity and causes high operating costs, technical difficulties, and flight delays and cancellations.
- Historical liabilities have created liquidity and solvency constraints.

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- Inadequate management of the company and lack of expertise resulted in low productivity, inefficient utilization of human resources and fleet of Air Serbia, as well as the absence of a revenue management system.
- Unfavorable business conditions over the last several years imposed additional pressure on passenger volumes and margin. These refer to: the recession in the Eurozone countries, increased costs of fuel, and entry of low-cost air carriers into the market.

The Fleet Does Is Not Fit For Purpose – Resulting in Significant and Increasing Problems in Maintaining the Profitability of the Network

An outdated fleet causes operational and financial problems:

- Aircraft require significant maintenance and are prone to technical failures
- low fuel efficiency

Air Serbia's pre-restructuring network was not designed to maximize connectivity with international destinations' network and traffic flow.

Historic Liabilities – High Levels of Debt Have Prevented the Business from Reshaping

High levels of debt – as of December 2012, Air Serbia's total financial debt amounted to USD [...].

Historic Liabilities – Inefficient Working Capital Management Has Meant that more than USD [...] of Trade Payables Were Outstanding for more than 30 Days. This Position Further Deteriorated in 2013.

USD [...] of unclassified trade payables were assumed to be overdue (in line with aged creditor data).

As of December 2012, Air Serbia owed substantial amounts, in particular to government entities:

- Airport ground handling: Total debt of USD [...] vs. est. annual expense of USD [...]
- Navigation: Total debt of USD [...] vs. est. annual cost of USD [...]
- Aircraft maintenance: Total debt of USD [...] vs. estimated annual cost of USD [...]

Historic Liabilities – Air Serbia Has Struggled to Raise Capital as Highlighted by Three Unsuccessful Attempts to Privatize the Firm

Air Serbia's difficulties in raising private capital have restricted the airline's ability to operationally restructure, become sustainable, and return to profitability. The situation is aggravated by the significant funding constraints facing the Government of the Republic of Serbia.

Weak Internal Governance and Expertise Has Undermined Efficiency

- Oversized and underutilized workforce – Air Serbia's workforce was severely overstaffed and underutilized.

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- Lack of hedging of fuel prices and foreign exchange – Air Serbia has been exposed to market price volatility in the jet fuel market and foreign exchange rates,
- Low utilization of aircraft – in May 2013, [...] of the Boeing 737-300 fleet was out of service. The average utilization of the Boeing 737 fleet between March 12 and Feb 13 was [...] hours per day, significantly lower compared to the European average of more than 10.5 hours per day,
- Insufficiently trained staff resulted in operating inefficiencies,
- Lack of yield management – Air Serbia did not have in place yield management systems to maximize revenues and profits,
- Small operator – Air Serbia's relatively small size gives the operator less bargaining power over procurement, increasing costs with suppliers,
- JAT Tehnika – Air Serbia historically received poor service and rates from JAT Tehnika.

Recent Unfavorable Trading Conditions

- Serbia's unemployment rate of 25% and fiscal strain due to a shrinking population, have also negatively impacted demand for air travel.
- Rising fuel costs have led to increased operational costs for Air Serbia. The lack of fuel efficiency of Air Serbia's aged fleet (aircrafts A319/320s) and strategies to optimize fuel usage have added to the impact of the rise in fuel prices for Air Serbia.

Recent Unfavorable Trading Conditions (Continued)

- Air Serbia has felt pressure on prices, particularly from LCCs entering the Serbian market.
- Whilst Air Serbia's load factors increased from [...] between 2010 and 2012, competition from LCCs has constrained growth in Air Serbia's load factors.

Air Serbia Would Not Be Able To Return To Long-Term Viability without Aid and a Private Investor

In early 2013, Air Serbia developed a 5 year plan, which did not include restructuring aid or a private sector partner.

Air Serbia would have encountered difficulties in implementing the plan and restoring the airline to long-term viability on its own.

4. Etihad-Air Serbia Partnership

On 1 August 2013, Etihad Agreed With the Government of the Republic of Serbia to Purchase a 49% Stake in Air Serbia

- As part of the proposed transaction, Air Serbia and Etihad developed a strategic plan to restore Air Serbia to profitability. This is an integral part of the transaction that sets out the various

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operational and financial restructuring measures that will be taken to make Air Serbia a sustainable business.

Etihad will use its expertise to help Air Serbia under a support services contract [...].

According to the Restructuring plan, the period between 1 August 2013 (announcement of Etihad and the Government of Serbia agreement) and Q1 2014 (closing date of transaction) is referred to as the transaction period. The period following Q1 2014 is referred to as the post-transaction period.

Etihad Entered Into a Support Services Agreement with the Government of the Republic Serbia [...]

On 1 August 2013 Etihad entered into a Support Services Agreement with the shareholders of Air Serbia [...].

According to the Rescue and Restructuring Plan, Air Serbia's Partnership with Etihad Is Expected to bring about a Range of Benefits that Are Critical to Restoring Air Serbia to Viability

Corporate Governance:

- Etihad will bring strong private sector governance to improve efficiency and decision making,
- Etihad will provide support with regard to the day to day management of the business,
- Etihad will appoint up to four members of the board, including Vice Chairman. Remaining members, including the Chairman, to be appointed by the Government of the Republic of Serbia,
- Best practice corporate governance to be introduced, including Manual of Authority which includes policies dealing with authority levels for employees and senior and a business ethics policy and code of conduct.
- Etihad representative to sit on the audit committee.

Network and Fleet:

- Etihad's expertise used to re-optimize the Air Serbia network with focus on serving regional markets and key European markets,
- Utilize Etihad's hub for services to the Middle East, Africa and Australasia,
- Utilize the Air Berlin and AF/KLM networks for secondary European airports,

Private Sector Funding:

- Etihad will provide the scrutiny of a private sector investor that seeks to restore the airline to long-term viability,
- Etihad's previous investments have improved the market's views of the airline (e.g., Air Berlin) and enabled it to raise third party funding.

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Joint Procurement and Operational Synergies:

- Etihad will bring increased bargaining power in renegotiation of all major supplier contracts at hub and outstations and consolidation of global procurement to leverage volume discounts,
- Etihad's commercial expertise will be used to implement fleet renewal plan,
- Revenue synergies: code share between Air Serbia and Etihad, Air France, KLM and Air Berlin; new Etihad Abu Dhabi – Belgrade route. Both allowing Air Serbia access to a larger network of cities without the cost of having to provide extra flights,
- Reworked Air Serbia European operations: rationalization of headcount through utilization of Etihad resources; [...]
- Air Serbia to gain from common IT Platform with Etihad Group; Reservations hosting, ERP systems, Revenue Accounting and Processing Center, Airport Departure Control and Flight Planning,
- [...]

5. Measures of the Government of the Republic of Serbia

5.1 Historical Measures

Air Serbia Has Accumulated Large Amounts of Historical Debt

- Air Serbia's net debt at 31 December 2012 was estimated at USD [...], including: bank debt (covered by guarantees issued by the Government of the Republic of Serbia), bank debt due to the Serbian National Bank, State-owned creditor balances and intercompany loans.
- The financial position of the airline has materially worsened since December 2012. Projections suggest that net debt could reach USD [...] by Q1 2014. Part of this debt of USD [...] has been identified as public debt (i.e. debt owed to government entities and state owned businesses and debt covered by state guarantees). This public debt of USD [...] has already been recognized and accounted for by the Treasury Department of the Government of the Republic of Serbia.
- Further, a proportion of Air Serbia's historical debt (USD [...]) was incurred prior to the State Aid Act enactment in 2010. Since this Act does not have retrospective effect, the debt incurred prior to that date should be excluded from the calculation of the amount of State aid provided by the Government of the Republic of Serbia, as stated in the Restructuring Plan.
- As part of Etihad's private capital investment, the Government of the Republic of Serbia has agreed with Etihad to rectify Air Serbia's financial situation before the transaction closes. The Transaction Framework Agreement (TFA) indicates that the Government of the Republic of Serbia shall be responsible for any liabilities, either individually or in aggregate relating to the operation of the airline prior to Q1 2014, whether they become due prior to or after Q1 2014. It is stated in the Restructuring Plan that this measure was necessary to attract a private investor that could enable Air Serbia to focus on operational restructuring measures in the medium-term rather than focus on covering historical liabilities.

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These historic liabilities need to be assumed by the Government of the Republic of Serbia:

- Financial liabilities: bank debt comprises USD [...], USD [...] disputed debt and USD [...] of other short term bank loans; and (ii) the Government of the Republic of Serbia liabilities comprise USD [...] debt to National Bank of Serbia (disputed) and USD [...] the Government of the Republic of Serbia loan.
- Overdue trade payables: consist of debts outstanding for more than 30 days (largest twenty suppliers, including handling, navigation and maintenance). A proportion is owed to government entities. USD [...] of unclassified trade payables assumed overdue.
- Other liabilities comprise deferred tax liability (the Government of the Republic of Serbia), amounts owed to group companies (the Government of the Republic of Serbia), unpaid wages (settled in January 2013) and provisions.
- Estimated cash burn to June 2013 based upon Etihad estimates (using prorated internal cash flow from sensitized Air Serbia strategic plan).
- Restructuring costs: comprise of cash expected to be received from the Government of the Republic of Serbia to fund redundancy costs (USD [...]) and aircraft lease deposit (USD [...]). An updated estimate of these restructuring costs would constitute part of the aid package and not part of historic liabilities.
- Based on Air Serbia's calculations, a total debt of USD [...] had been accumulated up to December 2009, that is prior to the enactment of Serbian State Aid Law. Excluding USD [...] of redundancy costs and aircraft lease deposits, Air Serbia is expected to have accumulated up to USD [...] of debt between January 2010 and Q1 2014.

5.2 Restructuring During Transaction Period

A Variety of Restructuring Measures Are Expected To Be Undertaken During the Transaction Period

As part of the proposed transaction, Etihad developed a strategic plan for Air Serbia. This is an integral part of the transaction that sets out the various operational and financial restructuring measures that will be taken between August 2013 and December 2016 to turn Air Serbia into a sustainable business.

The total cost of restructuring between 1 August 2013 and Q1 2014 is at least USD [...].

The Transaction Period Measures Will Be Funded By Etihad and the Government of the Republic Of Serbia

Etihad

Between 1 August 2013 and Q1 2014, Etihad will provide a short-term USD [...] shareholder loan to Air Serbia. The loan will provide access to cash in order to fund Air Serbia's on-going operations.

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The funding provided by Etihad and the Government of the Republic of Serbia prior to the transaction's closing date may, be used for the funding of: engine and aircraft lease deposits, rebranding costs and funding of ongoing working capital requirements prior to the transaction closing date (Q1 2014).

In addition, under the Support Services Agreement, Etihad is providing various services to Air Serbia on an on-going basis. These services include but are not limited to:

- Marketing measures,
- Yield management,
- Development of a call center and contact center strategy,
- E-Commerce: website rebranding and social media sites,
- Human capital investment from Etihad to Air Serbia during transaction period estimated at [...].

Total contribution by Etihad/Air Serbia during transaction period = USD [...].

The Government of the Republic of Serbia

Between 1 August 2013 and Q1 2014, the Government of the Republic of Serbia will fund the following restructuring activities:

- Reduction of headcount: Redundancy costs are expected to range from USD [...] to USD [...]. All redundancy costs will be funded by the Government of the Republic of Serbia. This includes the cost of all employment-related liabilities including redundancies, providing reasonable assistance in obtaining the consent of the trade union(s) to any redundancy program, pension and retirement benefits, legal costs, and outplacement training costs.
- Guarantee on Etihad's loan: Etihad's shareholder loan is guaranteed by the Government of the Republic of Serbia and hence this guarantee is categorized as an aid measure. This guarantee is expected to expire when the loan is converted into shares (when the transaction closes in Q1 2014). Simultaneously, in order to enable the restructuring of Air Serbia, Etihad is expected to provide Air Serbia with a shareholder loan of USD [...]. This loan is expected to be guaranteed by the Government of the Republic of Serbia [...]. The guarantees for the two loans do not overlap – this is equivalent to a single guarantee being in place at any point in time over the transaction and restructuring period. Hence, a value of USD [...] has been added as contribution by the Government of the Republic of Serbia for this loan guarantee.

Total contribution by the Government of the Republic of Serbia during transaction period is at least USD [...].

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5.3 Restructuring after Transaction Period

Etihad and the Government of the Republic of Serbia Plan Jointly To Invest In Air Serbia's Restructuring Plan in the Post-Transaction Period

- Etihad and the Government of the Republic of Serbia agreed that the privatization of Air Serbia will be followed by a corporate restructuring process to ensure that Air Serbia becomes a viable firm in the long-run.
- The management expertise of Etihad, its financing capabilities, its network and fleet as well as operational synergies are essential for Air Serbia's restoration to viability.
- The total restructuring cost after the Q1 2014 (the closing date of the transaction) is estimated at USD [...].
- The future shareholders of Air Serbia have further agreed to share the burden and risk of Air Serbia's restructuring measures.
- The measures listed below present significant steps to restore Air Serbia to long term viability.
- In the post-transaction period (after Q1 2014), contributions are expected to be made through shareholder loans and grants and the delivery of procurement savings by Etihad. Etihad's contributions (as a shareholder) to Air Serbia's restructuring plan in this period should be considered as at least equal to the contribution of the Government of the Republic of Serbia, as stated in the Restructuring Plan.
- The State aid measures in the context of the restructuring are limited to the minimum necessary so that in future Air Serbia can continue operating on its own merit.

The Costs Will Be Covered Jointly With a Significant Contribution from Air Serbia's Private Investor Etihad

- After the closing date of the transaction, Etihad will provide shareholder loans matching the funding provided by the Government of the Republic of Serbia: [...] in the year ending 31 December 2014; and USD [...] in the year ending December 2015.
- Further, Etihad will provide a Shareholder Loan to fund 50% of the cost of upgrades and enhancements to Air Serbia's light and line maintenance capabilities amounting to [...].
- Etihad will provide a Shareholder Loan to fund 50% of the cost of upgrades and enhancements to JAT Katering's capabilities subject to an overall limit of USD [...]. In addition Etihad will fund 50% of the cost of upgrades and enhancements to Su-Port's capabilities limited to USD [...].
- Etihad will continue to provide human capital investment to Air Serbia equivalent to approx. USD [...] over the five year period 2014-2018.
- Etihad's equity involvement will deliver contributions through savings in major aircraft contracts. Air Serbia's recently signed aircraft lease agreements [...]. Etihad's involvement delivers approx. USD [...] of savings for Air Serbia over the lease period.
- As part of the longer term investment in Air Serbia, Etihad has secured orders for 10 x A320 Neo aircrafts ([...]). These orders have been secured at discounted rates which Air Serbia would not have achieved on a standalone basis. [...].

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- Etihad's relationship with Airbus will help Air Serbia monetize a USD [...] Pre-Delivery Payment (PDP) that Air Serbia had paid to Airbus in 1998 in relation to an old aircraft order that was never fulfilled. With Etihad's involvement and relationship with Airbus, this amount is now being made available for Air Serbia to utilize against a future aircraft order.
- In sum, Etihad's equity involvement in Air Serbia is expected to deliver contributions through savings in major contracts, new aircrafts, and PDP. This participation reduces the costs to be faced by Air Serbia in the restructuring period (which it otherwise would have to finance) and may therefore be regarded as contribution to the restructuring costs.
- Air Serbia will contribute USD [...] through leasing their aircraft each year between 2014 and 2018.
- Air Serbia is expected to raise approximately USD [...] of revenues through the sale of properties. This amount has been added as a contribution from Air Serbia.

Total contribution by Etihad/Air Serbia after transaction period = USD [...].

The Government of the Republic of Serbia

- The Government of the Republic of Serbia will provide grants or by way of reducing operating cash expenses borne by Air Serbia (including passenger tax waivers at Belgrade airport): USD [...] in the year ending 31 December 2014; and USD [...] in the year ending 31 December 2015.
- Further The Government of the Republic of Serbia will provide a Shareholder Loan to fund 50% of the cost of upgrades and enhancements to Air Serbia's light and line maintenance capabilities amounting to USD [...].
- The Government of the Republic of Serbia will provide a Shareholder Loan to fund 50% of the cost of upgrades and enhancements to Katering's capabilities subject to an overall limit of USD [...].
- In addition, the Government of the Republic of Serbia will fund 50% of the cost of upgrades and enhancements to Su-Port's capabilities limited to USD [...].
- Between Q1 2014 and 31 December 2016 (inclusive), The Government of the Republic of Serbia will provide each year USD [...] as grants to Air Serbia to cover for cash shortfalls, supporting Air Serbia's working capital requirements. No further operative subsidies will be expected beyond the year 2016, when restructuring will be completed.

Total contribution by The Government of the Republic of Serbia after transaction period = USD [...] (excluding the value of the UDD [...] loan guarantee which continues from the previous period).

A majority of the post-transaction restructuring aid will be invested to improve Air Serbia's asset base.

The Government of the Republic of Serbia and Etihad will each fund 50% of the cost of upgrades and enhancements to Air Serbia's light and line maintenance capabilities.

The Government of the Republic of Serbia and Etihad will jointly fund the cost of upgrades and enhancements to Su-Port's and JAT Katering's capabilities.

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Table 1

Detail of The Government of the Republic of Serbia ', Etihad's, and Air Serbia's Contributions

| Measures | Restructuring Costs | Government measures (State Aid) | Etihad/Air Serbia's Own Contribution |
|---|----------------------------|--|---|
| Historical Measures | | | |
| Historic debt | [...] | [...] | - |
| Transaction period (2013-Q1 2014) | | | |
| Headcount reduction | [...] | [...] | - |
| Short term operating loan | [...] | - | [...] |
| Human Capital | [...] | - | [...] |
| The Government of the Republic of Serbia guarantee on Etihad shareholder loan | [...] | [...] | - |
| Restructuring after transaction (Q2 2014-2018) | | | |
| Shareholder loans/Grants | [...] | [...] | [...] |
| Air Serbia light and line maintenance upgrade | [...] | [...] | [...] |

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| | | | |
|---|-------|------------|------------|
| Katering and SU-port capability enhancements | [...] | [...] | [...] |
| Human capital investment 2014 - 2018 | [...] | - | [...] |
| Savings on major aircraft contracts | [...] | - | [...] |
| Savings on new aircraft purchases | [...] | - | [...] |
| Airbus PDP | [...] | - | [...] |
| Replacement Aircraft Leasing Costs | [...] | - | [...] |
| Sale of Air Serbia properties | [...] | - | [...] |
| Total | [...] | [...] | [...] |
| % | | 46% | 54% |

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Summary of Etihad's and the Government of the Republic of Serbia's contributions

- Etihad and the the Government of the Republic of Serbia are both contributing significantly to the restructuring costs of Air Serbia.
- Air Serbia's historical liabilities accumulated since the enactment of Serbian State aid law in 2010 are equal to USD [...].
- Air Serbia is also contributing to the restructuring costs by scrapping old aircraft and selling assets (like real estate). As the amount of the proceeds is not yet established, these are not taken into account in the calculation of the own contribution. Nonetheless these measures reduce the aid amount to the minimum necessary and help restore Air Serbia to long term viability.

Table 2

| | Total Restructuring Costs | Government measures (State Aid) | Etihad/Air Serbia's Own Contribution |
|--|----------------------------------|--|---|
| Historical measures (until Q1 2014) | [...] | [...] | - |
| Transaction period (August 2013 to Q1 2014) | [...] | [...] | [...] |
| Transaction period (August 2013 to Q1 2014) | [...] | [...] | [...] |
| Total | [...] | [...] | [...] |
| % | | 46% | 54% |

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6. Restructuring Measures

Air Serbia, together with Etihad, has developed a restructuring plan that aims to address the issues that led it to become a 'firm in difficulty'. The plan seeks to restore Air Serbia to long-term viability.

Measures under Air Serbia's Restructuring Plan suggest that in the baseline case Air Serbia is expected return to profitability within three years.

Air Serbia has also identified two downside scenarios and assessed whether the business can return to profitability under these scenarios: fuel price shock; and increased competition from LCCs on Air Serbia routes. Management tested these scenarios and discussed potential strategies to manage these risks. The modelling results suggests that Air Serbia is expected to have sufficient cash in each year to withstand the losses incurred in these scenarios and not require additional State aid in the future.

Restructuring measures have been divided into a number of activities: network planning, headcount reduction, fleet replacement, new governance structure, procurement synergies and other measures such as commercial and rebranding strategy.

Air Serbia plans to offer an improved product proposition.

Modelling of the Restructuring Plan

Various inputs were used to understand the impact of the restructuring plan on the future viability of Air Serbia

Viability of Air Serbia's Restructuring Plan Was Stress Tested under a Baseline and Downside Scenario

Baseline Scenario

In a baseline case, Air Serbia is expected to return to profitability within three years. No operative subsidies are required post-2016, when the business is expected to reach profitability. This is reflected in the financial projections which do not rely on any such subsidies.

Viability of Air Serbia's Restructuring Plan Was Also Stress Tested under Two Downside Scenarios

The restructuring plan considers two possible downside cases:

- Fuel price shock; and
- Increased competition from LCCs on to Air Serbia routes.

Viability has been assessed as Air Serbia's ability to absorb a shock in revenue or costs (i.e. cash buffer in each year between 2014 - 2018) and avoid seeking future State aid.

These downside scenarios were war-gamed by Air Serbia's management to determine what the company risk and response would be in each case. (i.e. mitigation strategies).

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Fuel Price Shock – Air Serbia should have sufficient cash to absorb a [...] increase in fuel prices.

Increased competition from LCCs on to Air Serbia routes – competition from LCCs is likely to continue and place greater pressure on yields.

Increased competition from LCCs on to Air Serbia routes – Air Serbia should have sufficient cash to absorb a [...] reduction in yields on routes that are most vulnerable to competition from LCCs.

Air Serbia plans to adopt several strategies to mitigate potential losses in a Downside scenario.

The restructuring package is necessary to avoid significant social hardship in the Republic of Serbia.

The restructuring aid, therefore, pursues a common interest in that it aims to prevent social hardship by restoring the long-term viability of Air Serbia.

The Aviation Industry Plays a Critical Role in the Economic Development of Serbia and the Promotion of Belgrade as a Hub for the Eastern European Market

Role of air transport:

- Air transport is a significant element of general economic development and allows for spatial integration of all processes of economic activity, from manufacturing to services. It significantly contributes to the production and exchange of material goods, technical and technological development as well as supporting employment through the transfer of labor.
- The EU has pursued a clear strategy of enhancing connectivity, integration and trade in the Single Market through promoting air transport.

The Social Cost to the Republic of Serbia of the Failure of Air Serbia Would Be Enormous.

7. Competition Concerns

The total number of passengers carried in Europe in 2012 amounted to 826 million. Air Serbia flew approximately [...] passengers in 2012, representing less than [...] of the European market. In terms of direct seat capacity, Air Serbia also accounted for less than [...] of the European market in 2012.

The fleet replacement will result in a reduction of [...] in passenger seat capacity.

As stated in the Rescue and Restructuring Plan, the current route and fleet reconfiguration for Air Serbia constitute a network which is necessary to achieve and maintain viability in the long-run. High fixed cost base of the airline operation does not allow a reduction in the operations presented in the Rescue and Restructuring Plan without jeopardizing the sustainability of the airline going forward.

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III. Commission Decision

At its 66th session, held on 21 February 2014, the Commission adopted a decision allowing for the grant of restructuring aid to Air Serbia, which was included in the Restructuring Plan.

The Commission has concluded that the Restructuring Plan, with all appendices and schedules which were submitted as its integral parts, has been made in accordance with the Act and the Regulation.

During its deliberations, the Commission took into account the fact that the Agreements represent:

- An actual or potential public expenditure, or net realization of public revenue,
- A selective measure, as it provides a market advantage to the individual aid beneficiary i.e. Air Serbia,
- A measure that distorts or may distort competition on the market,
- A measure that affects free competition on the market,

which means that this is a case that constitutes state aid (Article 2 item 1) of the Act.

The Agreements represent a ground for allocation of individual state aid, given that the aid beneficiary is pre-determined, in terms of Article 12 paragraph 3 of the Act.

Air Serbia does not operate in the steel and coal sectors and it is not a newly established company; therefore, it is possible to grant restructuring aid, pursuant to Article 21 paragraphs 1 and 2 of the Regulation.

In addition, the Commission has examined whether the conditions prescribed under Article 23 paragraph 1 of the Regulation were cumulatively fulfilled: did the company prepare a restructuring plan, whether the company undertook compensatory measures in order to avoid significant market disruptions and whether the aid amount was limited to the minimum necessary for the implementation of the measures under the Restructuring Plan.

The Commission has analyzed the Restructuring Plan in a number of aspects: a test of sustainability, a minimum amount and intensity of state aid, own contribution and compensatory measures.

Taking into account that the Restructuring Plan includes financial projections for the restructuring period, the Commission finds that the return to the long-term viability and competitiveness of the company is plausible, and that the planned three-year-period is reasonable.

In addition, the Commission particularly appreciated the termination of loss-making activities, and that the most important restructuring measures (leading to sustainability) were implemented in the first period of restructuring, as well as the compensatory measures.

The Commission, furthermore, has found that the Restructuring Plan contained a detailed description of internal and external circumstances that led to business difficulties, current market conditions and future assessments of supply and demand. Moreover, the Restructuring Plan included assessments, and different

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scenarios of market trends, as well as a description of strengths and weaknesses of Air Serbia, i.e. positive, synergy effects of Etihad's entry into the ownership structure and management of Air Serbia.

The Commission has paid particular attention to the description of the causes, difficulties, problems, importance and conditions within Air Serbia, in order to determine whether the measures proposed in the Restructuring Plan were adequate. The Commission has concluded that the Restructuring Plan was unambiguous and that it contained unambiguous and sufficiently clearly defined restructuring measures and time required for the restructuring of Air Serbia, and that it was based on actual assumptions of future business activities, since its aims were realistically and plausibly set, i.e. achievable. Therefore, based on the factual description that led to Air Serbia's difficulties, the Commission has estimated that the proposed measures were appropriate.

Furthermore, the Restructuring Plan provides for a liquidation of organizational units that caused losses, including social measures in favor of redundancy, therefore the Commission concluded that these measures were aimed at solving problems and establishing viability through internal i.e. organizational restructuring, as a key part of the restructuring.

The Commission has appreciated the financial projections envisaged under the Restructuring Plan, which did not rely on state aid after 2016. This means that it is expected that Air Serbia returns to viability and competitiveness in a three-year-period, which also means that state aid for funding of business operations will not be needed beyond 2016, since the envisaged organizational form will enable Air Serbia to cover all of its costs after the restructuring, including depreciation and financial liabilities, all without additional aid.

The Commission has particularly appreciated the different scenarios that were presented with respect to market trends, competition, current and future business risks.

Since some of the restructuring measures have been already implemented (e.g., downsizing), and the remaining measures will be implemented during the defined restructuring period (three years, as provided in the Restructuring Plan), the Commission believes that Air Serbia can return to long term viability. A variety of operational and financial restructuring measures will be implemented during the period from August 2013 to December 2016, in order to restore long term viability of Air Serbia, which means that the start and end of the restructuring process are specified, thus fulfilling the requirement of Article 23 paragraph 1 item 1), sub-item (d) of the Regulation.

Article 23 paragraph 1 item 2 of the Regulation contains a provision stipulating that the recipient of restructuring aid ought to undertake compensatory measures to avoid significant market disruption. A compensatory measure includes: transfer or sale of assets, decrease of capacity or market share reduction.

When analyzing the measures provided in the Restructuring Plan, the Commission has examined whether the requirements set forth in Article 23 paragraph 1 item 2) of the Regulation were met. Bearing in mind that compensatory measures are necessary in order for the intended beneficial effects to outweigh the detrimental effects, the Commission analyzed whether the measures proposed in the Restructuring Plan

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(sale of [...] and [...] properties in the Republic of Serbia, as well as offices in the territory of: [...]) were proportional to the distortive effect on competition at the market.

In assessing whether competition would benefit from the proposed compensatory measures, the Commission has particularly taken into account the fact that these measures would be implemented in the markets at which Air Serbia would, following the restructuring, have a significant market position, i.e. a significant share. The Commission has also appreciated the size and position of the company in the relevant market and has concluded that the proposed measures were adequate, especially in relation to the relative importance (share) of the state aid beneficiary on the market.

Therefore, the Commission considers that the compensatory measures are proportionate to the assessment of the negative distortive effects on competition and expects that granting of state aid to Air Serbia will have a minimal negative impact on competition, as opposed to option of a definite exit of Air Serbia from the market.

The Commission has also taken into account the fact that the Restructuring Plan states that following the restructuring process of Air Serbia, it plans to reduce seat capacity by approximately [...], which in the long term, also constitutes a form of a compensation towards competition.

The Commission has not considered debt cancellation and termination of loss-making activities as capacity reduction, or reduction of market share, because the aforementioned were necessary to restore profitability of Air Serbia.

In order to limit the negative impact on competition in the market, the Commission has assessed whether the amount of state aid was limited to the minimum necessary for the implementation of the measures under the Restructuring Plan while remaining certain no surplus funds were granted to Air Serbia, which it then be able to use for other activities not related to the restructuring process. The Commission has concluded that the amount and intensity of state aid provided for under the Restructuring Plan was limited, i.e. minimum, and was in the amount necessary to achieve the objectives of the restructuring and return to long-term viability/profitability.

Therefore, the Commission concluded that the concept of proportionality, determined by state aid intensity, was met and it ensured that the state aid amount was not excessive, i.e. that it was in line with the objectives of the Restructuring Plan.

In accordance with Article 23 of the Regulation, state aid for restructuring may be granted, inter alia, if the state aid beneficiary shares the burden and funds a portion of the costs pertaining to the restructuring process from its own resources or from external financial sources under market conditions, as follows: a small enterprise in the amount of at least 25%, a medium enterprise in the amount of at least 40% and a large enterprise in the amount of at least 50%. Own contribution is proof that the company itself, its shareholders and the market, all believe in the recovery and the possibility of establishing a commercially profitable business and that they accept the risk of investing and financing such a firm. Therefore, it is expected that this contribution was actual i.e. concrete and to be realized from the company's own assets

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which was not necessary for the survival of the firm in difficulty, as well as from capital investments or external sources (loans) under market conditions, i.e. without government guarantees.

Total restructuring costs of Air Serbia amount to USD [...] of which state aid amounts to USD [...], which constitutes 46% of the total restructuring costs, while the own contribution of Etihad and Air Serbia amounts to USD [...], which accounts for 54% of total restructuring costs.

The Commission finds that the granted state aid for restructuring, in the above mentioned amount, constitutes a minimum necessary amount of aid in the process of restructuring of Air Serbia, which is to be carried out in the period from 2013 to 2016.

During its proceedings, the Commission examined whether Air Serbia was funding a portion of the restructuring process costs from its own resources (or from external sources of financing under market conditions). Namely, the Commission assessed whether such a contribution was concrete, i.e. real, that is excluding all future expected profits, such as cash flow.

The Commission expected from the state aid beneficiary to contribute significantly to the process of restructuring from its own resources (including the sale of real estate), which would show confidence in the feasibility of its return to viability (profitability). Since the own contribution of Etihad and Air Serbia amounts to USD [...], which accounts for 54% of the total restructuring costs, the Commission concluded that it met the requirement of Article 23 paragraph 2 of the Regulation, which prescribes the intensity of own contribution for large enterprises to be at least 50%.

The Commission assessed that the Air Serbia's contribution was concrete, i.e. and real.

Further, the Commission analyzed the Restructuring Plan in order to determine if it was possible to return to commercially viable business activity, i.e. whether following the restructuring Air Serbia would be able to cover all operating costs, including depreciation and financial liabilities. In addition, the Commission particularly appreciated that the increase of profitability would stem from the measures intended to be taken within Air Serbia, which related to the structure of revenues and costs, and which would ensure that following the restructuring period, Air Serbia would continue to operate without further state aid. Moreover, the most important restructuring measures that should led to [return to] viability were implemented in the initial period of restructuring, which led the Commission to conclude that the proposed measures were feasible and appropriate, and that the possible negative scenarios were accounted for, together with the assessment of the market conditions in which Air Serbia would operate.

Thus, the Restructuring plan will lead to a return to long-term viability and competitiveness of Air Serbia, and the provided three-year-period represents a reasonable time, and, thus, the assumptions regarding future business conditions are to be deemed realistic, including the termination of loss-making activities pursuant to Article 23 paragraph 1 item 1) of the Regulation.

The Commission has considered that the aid was justified in view of the volatility of the Serbian market and that a potential collapse of Air Serbia would have a devastating impact on the economy of the Republic of Serbia as a whole. In addition, the Commission has found that Air Serbia exhausted its own strategies for risk reduction and could not recover using its own resources. Therefore, state aid for

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restructuring of Air Serbia is necessary in order to prevent the company from going out of business as well as the significant social hardship, which would be brought about to the Serbian economy under such a scenario.

The Commission finds that the entry of an investor as a means of additional source of available capital, which would alleviate future financing activities of Air Serbia (given the difficulties in which Air Serbia is presently), is an economically justifiable and a sustainable solution, in particular bearing in mind that the said investor has the knowledge and experience in the field of air transport.

Acting in accordance with the provisions of Article 24a of the Regulation, under the above paragraph 2 of this Decision, the Commission instructs the Applicant to submit to the Commission regular annual progress reports regarding the implementation of the Restructuring Plan, for the time until the completion of the restructuring process of Air Serbia, and to notify the Commission in writing that the restructuring process is complete, as soon as it receives such notification from Air Serbia.

In the light of the considerations above, the Commission has adopted the Decision as cited above.

Legal remedy: this Decision is final in administrative proceedings and subject to administrative dispute that may be initiated against it within 30 days as of delivery.

COMMISSION CHAIRPERSON

Ms. Inge Suput-Djuric

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To be delivered to:

- The Office of the Deputy Prime Minister
- The Archive