TAPGROUP

TAP – Transportes Aéreos Portugueses, SGPS, S.A. (Consolidation)

2016

MANAGEMENT REPORT

(MAIN FACTS)

AND

ACCOUNTS

A STAR ALLIANCE MEMBER

MANAGEMENT REPORT
(Main Facts)

2016

Economic Environment

International Environment

Throughout 2016, global economic activity kept the main traits which characterized it during 2015, and the global GDP is expected to grow around 3.1%.

In the advanced economies and following a moderate evolution of the economy during the first half of the year, a more significant recovery was registered during the second semester, driven mainly by a reduction in stocks and by a certain recovery in manufacturing production. In the emerging and developing market economies (EDME), and despite the high level of heterogeneity between countries, a slight improvement in prospects was noted throughout the first semester, but it was followed by an unexpected deceleration, reflecting idiosyncratic factors.

Among the advanced economies, in the United States, economic activity rebounded strongly after a weak first semester, with the economy moving close to a situation of full employment. In several other advanced economies, production remained below potential, but the numbers of the third trimester are a little stronger than initially expected in some economies such as Spain and the United Kingdom, where domestic demand rose above the expected after the Brexit vote. In Japan, historical revisions of growth suggest higher growth than anticipated in previous estimates.

As for the emerging and developing economies, growth in activity was slightly stronger in China than expected, driven by the continued political stimulus. On the other hand, it registered greater weakness in certain Latin-American countries that are currently in recession, such as Argentina, Brazil, the ever-deteriorating Venezuela, and Turkey, a country which has suffered a sharp reduction in tourism revenues. In Russia, activity was slightly better than expected, partially reflecting more sustained oil prices.

As far as prices are concerned, throughout the year and alongside the development of the non-energy component, energy goods registered lower levels than in 2015, estimating that the average price of a barrel of Brent crude oil went from 52.4 USD in 2015 to 43.1 USD in 2016. However, this trend changed in the last weeks of the year, reflecting an agreement between the main producers to cut supplies.

In the euro area, representing about 66% of external demand for Portuguese goods and services, the process of economic recovery continued, with an expected growth of 1.7% in 2016. The main contribution underlying this behaviour is made by internal demand, supported by the ECB's highly accommodative monetary policy stance, while net exports maintained a slightly negative contribution.

Among the items of internal demand, the impact of private consumption and of the Gross Fixed Capital Formation (GFCF) stands out, both of them in keeping with the value registered in 2015. The work market continued its recovery trend, but employment was still below pre-crisis levels in most countries of the area, and the unemployment rate remained above 10%, despite a slight decrease. The recovery in economic activity was generalized to most countries of the euro area, with differences in terms of pace.

In Spain, representing about 27% of external demand for Portuguese goods and services, and if the economy keeps up the previous year's pace, it is expected to have ended 2016 with a 3.2% evolution, boosted by private consumption but also by the GFCF, reflecting an improvement of the financial conditions and rising confidence of economic operators. As regards Germany, representing about 14% of external demand for Portuguese goods and services, following a 1.5% growth in 2015, the economy (usually evolving slightly above the euro area) is expected to end 2016 with a 1.9% growth, under the influence of a relatively stronger momentum of public consumption and of the GFCF. It should be noted that other large-scale markets in the European economy which are destinations of Portuguese exports, namely France and Italy, are expected to keep up the slight recovery pace registered in 2015, with increases of 1.3% and 0.8%, respectively. On the other hand, a continued reduction in the government deficit was registered in the euro area as a whole, with the public deficit ratio expected to reach 1.8% of the GDP in 2016.

National Environment

Following a growth of 1.6% in 2015, economic activity in Portugal should register a moderate growth, around 1.2%, in 2016, characterized by a less dynamic evolution of both internal demand and exports. Private consumption is expected to increase by about 2.1%, decelerating in comparison to the behaviour observed in the past few years, associated with the expenditure on durable consumer goods. It should be mentioned that, as a reflection of growing internal and external pressures, inflation is expected to grow about 0.8% (from 0.5% in 2015), in particular, thanks to energy and non-energy commodity prices, in a reversal of the downward trend seen in recent years. As regards the work market, in 2016 job growth is expected to continue as well as the growing trend of the unemployment rate, which is expected to reach 11.0%.

Additionally, after an increase of 4.5% in 2015, the GFCF is expected to fall by about 1.7%, in association with behaviours of the public component and of the residential component, the former partially explained by the delivery of sold military material. It should also be noted that the evolution of this component is particularly subject to uncertainty, thanks to the late entry into force of the budget and given the profile of the expenditure related to investment projects co-financed by Community funds. In turn, following a particularly dynamic growth in the export of goods and services in 2015 (6.1%), projections point to a deceleration of this growth in 2016 (3.7%), reflecting both the deceleration of external demand, certain temporary factors, a reduction in the production in industrial units of the automotive and energy sectors, and the unfavourable performance of sales to certain non-EU markets, namely Angola.

Corporate Governance

The information on the Company's Governing Bodies is available for consultation at the TAP Group's website www.flytap.com.

Governing Bodies

Three-year period 2015–2017

TAP–Transportes Aéreos Portugueses, SGPS, S.A.

General Meeting Committee

Chairman Diogo Patrício de Melo Perestrelo
Through deliberation at the General Meeting Committee on 8th March, 2016

Company Secretary Ana Maria Sirgado Malheiro
Pursuant to number 1 of article 13 of the Company's by-laws

Board of Directors

Through deliberation at the General Meeting Committee on 12th November, 2015

Chairman Humberto Manuel dos Santos Pedrosa
Member Fernando Abs da Cruz Souza Pinto
Member David Humberto Canas Pedrosa
Member Maximilian Otto Urbahn
Member David Gary Neeleman
Member Francisco Maria Freitas de Moraes Sarmento Ramalho
Member Henri Courpron
Member Philippe Calixte Albert Delmas
Member Robert Aaron Milton
Member Sydney John Isaacs
Member Tiago Gonçalves de Aires Mateus

Executive Committee

By election by the Board of Directors at the meeting on 13th November, 2015

Chairman Fernando Abs da Cruz Souza Pinto
Member David Humberto Canas Pedrosa
Member Maximilian Otto Urbahn

Company Secretary

By appointment of the Executive Committee, at the meeting on 16th December, 2015 ratified by the Board of Directors of the Company on 20th January, 2016 pursuant to article 23 of the Company's by-laws, effective 16th December, 2015.

Company Secretary Ana Maria Sirgado Malheiro
Alternate Company Secretary Not appointed

Supervision of the Company

Supervisory Board

The Supervisory Board of TAP, SGPS, S.A. was elected at the General Meeting on 12th November, 2015, for the three-year period 2015-2017, with the following composition:

TAP, SGPS, S.A.

Mandate (Start - End)	Position	Name	Appointment Doc.	Mandates held in the company	
				Number	Date of 1.st appointment
2015-2017	Supervisory Board	Sérgio Sambade Nunes Rodrigues	General Meeting Committee on 12th November 2015	1	12.nov.2015
		Baker Tilly, PG & Associados, SROC, S.A.	General Meeting Committee on 12th November 2015	1	12.nov.2015
		Maria Susana da Mota Furtado e Almeida Rodrigues	General Meeting Committee on 12th November 2015	1	12.nov.2015
	Alternate	António Pires dos Reis	General Meeting Committee on 12th November 2015	1	12.nov.2015

Official Accountant

Through deliberation at the General Meeting Committee on 30th May, 2016, for the remaining period of the current term 2015–2017

Permanent Oliveira, Reis & Associados represented by Joaquim Oliveira de Jesus
Alternate Fernando Marques Oliveira

Risk Management

Risk management and internal control

The model created by the European Community specifically separates areas, functions and professionals so that they can be efficiently and effectively coordinated, and clearly defines responsibilities and establishes the respective limits. This allows a clear view of the framework of the different positions in the organisation's general risk and control structure.

This model – the Three Lines of Defence Model – takes into account the following aspects:

Three Lines of Defence Model

1st Line of Defence – The person responsible for the business area, the direct manager, responsible for identifying, measuring, evaluating and mitigating the risks of the respective business. Each business unit has inherent operational risks and is responsible for keeping efficient, appropriate and effective internal controls and for implementing corrective actions to resolve deficiencies in processes and controls;

2nd Line of Defence – It includes the duties of risk management and compliance and should work together with the business area to ensure that the situations identified in the 1st Line of Defence have been properly evaluated and the business risks correctly reported;

3rd Line of Defence – It is represented by the Internal Audit, which should systematically and efficiently review, monitor and evaluate the activities of the first Lines of Defence and contribute to its improvement, enhancing its effectiveness.

This model decisively reinforces that the process owner is the owner of the risk and its controls. In this sense, frauds only happen when the process owners are not imbued with commitment and do not have the maturity to put into practice the controls and respective methodologies suggested and supervised by the second Line of Defence. As one of the three lines of defence in the TAP Group's risk management, Internal Audit seeks to evaluate and monitor the efficiency and effectiveness of operations, the preservation of assets, the confidence and integrity of reporting processes and the conformity with the law, regulations, policies, procedures and contracts established.

Giving continuity to the Corporate Risk Management (CRM) process, initiated and implemented in the 2nd semester of 2015 and applicable to all the companies of the TAP Group directly involved in operating and maintaining air transport activity, 155 risks were identified at the end of 2016. The Internal Auditing Office was given the responsibility of centralized monitoring, controlling and reporting of the CRM, which performs the treatment and monitoring of the Corporate Risk Management of the Company, in a coordinated and structured manner, as set out in the Corporate Risk Management Manual, using the COSO model and the FERMA analytical tool as the basis for assessment.

With the aim of strengthening the management, monitoring and evaluation of the compliance risk, the Company drew up the Compliance Manual, preferably reinforcing the areas to be monitored in the different Audits carried out over the year that form part of the Annual Audit Plan. In TAP Portugal, in order to prevent and avoid the violation of rules and the deviation of behaviours which have negative consequences for the organisation and for society, an area of Compliance was created, integrated in TAP Group's Auditing Office, aimed at embracing the implementation of good practices in the Group's businesses.

Following the disclosure of the Manual on Good Business Conduct, the Company made a compilation of national and international legislation applicable to Compliance, which culminated with the internal publication of the Global Compliance Manual. This document clarifies and is designed to align all of the organisation's processes in order to ensure compliance with standards and procedures, integrating anticorruption and ethical practices in TAP's culture. It is based on a responsible and conscious attitude of all of the Company's stakeholders. In this context and under the monitoring duty, the Audit enhanced the Compliance aspect, implementing best practices of Corporate Governance in its routines in all analyses carried out.

As a complement and due to its importance and cross-cutting nature, an internal communication channel was made available, aimed at a general involvement in the Compliance culture, clearing up doubts and reporting cases that are known to the various stakeholders of the TAP Group's organisation.

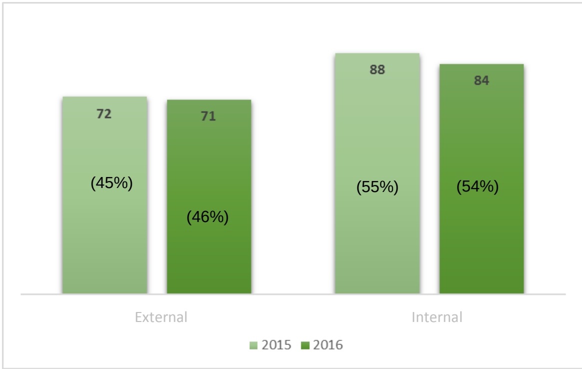
Risk factors and their management

Type of Risk

External Risks – Event that occurs due to external factors; the Company does not have any type of control and has to adapt to the new realities.

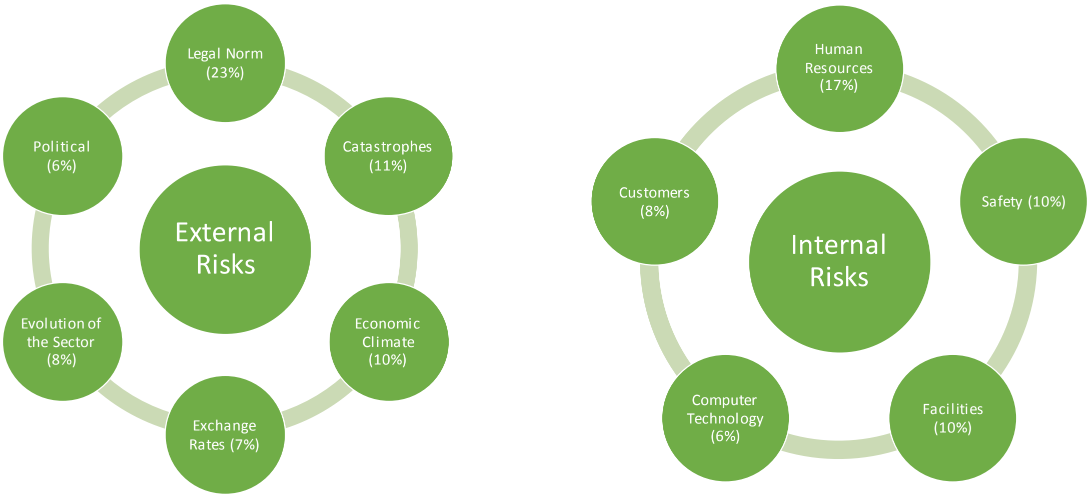
Internal Risks – Risk that is based on internal factors with which the company can interact in order to define a mitigation, acceptance, transfer or refusal strategy.

Distribution of the Type of Risk – TAP Group



INTERNAL RISKS						EXTERNAL RISKS	
ORGANISATIONAL	SUBSIDIARY PROCESSES	ISOLATED	CONTRACTUAL	FINANCIAL	OPERATIONAL	EXTERNAL	MARKET
▪ Human Resources ▪ Suppliers ▪ Customers ▪ Organisation Commercial ▪ Own brands ▪ Products ▪ Security ▪ Marketing ▪ Facilities	▪ IT ▪ Infrastructures ▪ Certifications ▪ Technical Factors ▪ Security ▪ Indemnities ▪ Mergers/ acquisitions	▪ Projects ▪ Subsidiaries ▪ Institutional Commitments ▪ Internal Control ▪ Social Responsibilities ▪ Fraud ▪ Corruption	▪ Buying Commitments ▪ Payment Guarantees ▪ Fraud ▪ Corruption	▪ Financial Assets ▪ Liquidity ▪ Interest Rates ▪ Exchange Rates ▪ Fuel Price ▪ Mergers/ acquisitions ▪ Indemnities ▪ Treasury	▪ Operational Risk ▪ Maintenance and Engineering Risk ▪ IT risk ▪ Fires and Prevention ▪ Health and Safety at Work	▪ Economic Environment ▪ Social Environment ▪ Interest Rates ▪ Exchange Rates ▪ Taxes ▪ Catastrophes ▪ Political ▪ Partnerships ▪ Epidemics	▪ Attractiveness of the Market ▪ Developments in the Sector ▪ Competition ▪ Distribution ▪ Commercial Organisation ▪ New Products ▪ New Technologies ▪ Legal Requirements
Risks in the Company's organisation (people and services) and in the interactions between the Company and suppliers/customers	Risks found in the processes/ activities supporting the Company's activity	Events that do not have a frequent routine in the Company's activity	Existing risks with the commitment between the Company and suppliers/ customers and existing mitigations	Systems and actions to monitor and control economic and financial risks; monitoring of economic and geopolitical developments, namely in countries with high social and political instability, and internal auditing procedures, contracting and transactions	Risk of financial losses or negative impacts on the business and/or on the organisation's image/reputation, caused by faults or failures in governance and business processes, in people, in the systems or resulting from external events that may be triggered by countless events	Risks related to the economic, environmental and social environments that are not directly related to the Company's activity	All events that may be translated as a risk to the Company's activity and that are directly related to its activity

Distribution, per type and main categories, of the 155 risks of the TAP Group, sent by the 20 protagonists involved in the process of collecting information for the Corporate Risk Management (CRM)



Risks of economic and financial nature

Systems and actions of monitoring and control of economic and financial risk, follow-up of economic and geopolitical development, particularly in countries showing high social and political instability, and internal audit of procedures, contracting and transactions.

Operational risk (Security | Safety)

Model of action whereby the possibility of damage to people and assets is minimised or eliminated, through a continuous process of identification of situations of potential danger and management of the respective associated risk.

Information technology risk

Systems used by organisations to identify weaknesses and threats.

Fire risk – prevention

Risk management system for fire, explosion and spillage of chemical products. The system includes the Internal Safety Plans, the Training of Employees, the Manuals for Protection against Explosive Atmospheres (ATEX Manuals), the Emergency Drill Exercises (fire, spillage of chemical products and earthquake) for the training of Employees and Emergency Support Teams (Safety, Surveillance and Fire Brigade Station), and an Internal Audit Plan.

Maintenance and Engineering risk

At TAP–Maintenance and Engineering, risk management is inherent and integrated in the responsibilities defined in the context of the aeronautical certifications and accreditations held [EASA Parte 145 (Maintenance Organisations); EASA Part M (Continued Aeronavigability); NP EN ISO 9001:2008 (Quality Management Systems), among others] which are compulsory to guarantee the continuity of its activity.

Occupational health and safety risk

Risk management system supported by the identification, assessment and control of professional risks, with repercussions on health and safety, aimed at improving health and the quality of life of individuals and of society, fostering productivity, through the involvement of the entire Company in a Risk Prevention Culture.

Summary of Performance of TAP–Transportes Aéreos Portugueses, SGPS, S.A. (Consolidation)

In 2016, the air transport business continued to make a decisive contribution to the development of the world economy, promoting connectivity through the establishment of over 700 new routes, and providing over 4 billion passengers with opportunities for growth, through the positive impacts of globalization – encouraging innovation and creating business opportunities. On a global level, passenger demand in terms of passenger-kilometre totals suffered a development of around 6.3% compared to 2015, a result which significantly surpassed the yearly average of a 10-year period, situated at around 5.5%, while the capacity offered increased by 6.2%. The seat load factor, rising 0.1 p.p., reached an all-time high, at around 80.5%, justifying airline companies' investment in maximizing the capture of demand. Throughout the year, a slowdown took place regarding the intense pressure on the yield, though the downward trend continued, allowing air travel to become even more accessible. Regarding the air cargo market, global traffic increased 3.8% in 2016, recovering in the second semester, and almost doubling the average growth rate of the Industry, around 2%, recorded in the last five years.

Meanwhile, aircraft fuel prices, after further declines in oil prices in December 2015 and January 2016, resumed an upward trend throughout the year. Notwithstanding this trend, which was sharply accentuated in early December 2016, following the agreement by non-OPEC suppliers to accompany their counterparts in that organization in limiting supply, it is estimated that the average price of Brent crude oil barrel evolved from 52.4 USD in 2015 to 43.1 USD in 2016.

As a result of this behavior, the overall fuel charge for TAP, S.A., which still accounts for a significant portion of the company's total Operating Expenses and Losses (in the order of 20%), decreased by 34.3% in relation to 2015, equivalent to EUR 226.5 million, and the oil price performance had a favorable impact on TAP's fuel costs, estimated at EUR 200.5 million.

Fuel Costs TAP, S.A.

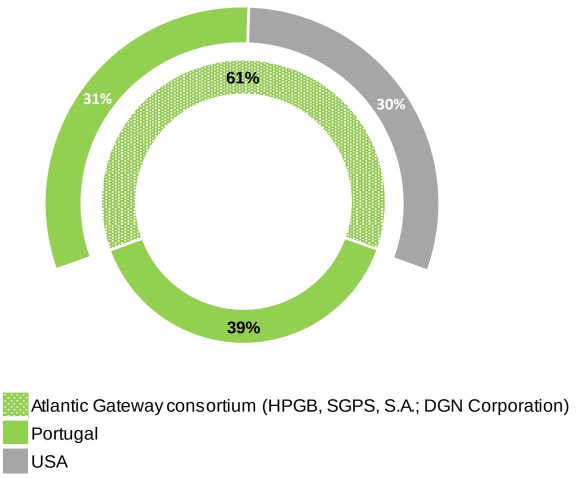
EUR million	2016	2015	var. (abs.)
Total (*)	**433.8**	**660.3**	**-226.5**
Price Effect			-200.5
Quantity Effect			-20.7
Aquisition of the CO_2 emission Allowances	0.7	5.9	-5.1

(*) Includes charges relative to the acquisition of the CO_2 emission allowances

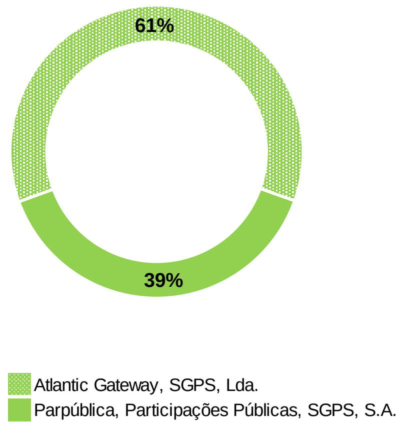
Shareholder structure of the TAP Group on 31 December, 2016

Geographical distribution and by type of investor of the shareholder structure of TAP−Transportes Aéreos Portugueses, SGPS, S.A., on 31 December 2016

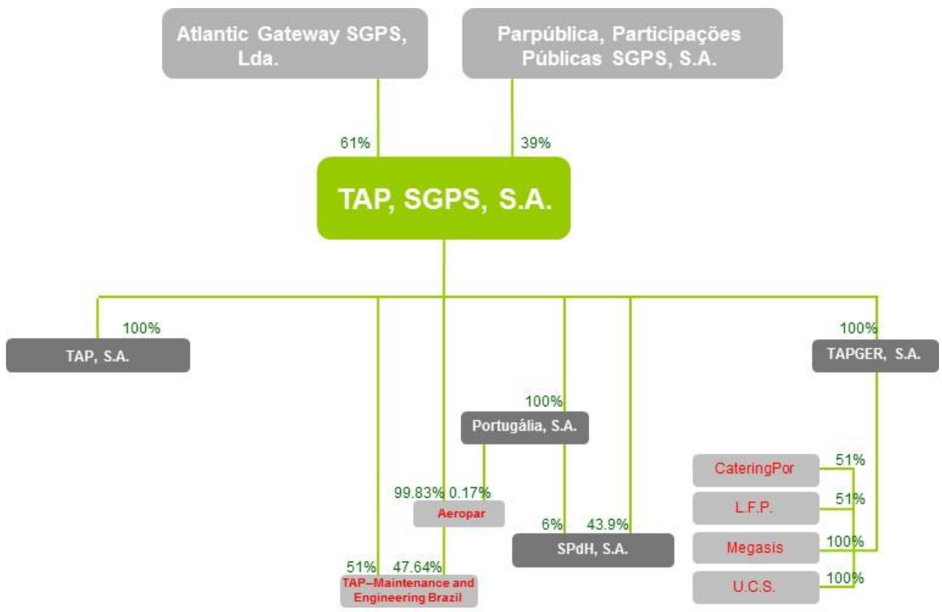
Geographical distribution of the shareholder structure



Breakdown of the shareholder structure by type of investor



At the end of 2016, the Group of companies that were part of the consolidation perimeter of the TAP holding was made up of TAP–Transportes Aéreos Portugueses, SGPS, S.A. and its subsidiaries, according to the organisational diagram.



Consolidation methodology

As at 31 December 2016, the following companies were included in the consolidated financial statements by the full integration method:

- TAP–Transportes Aéreos Portugueses, SGPS, S.A.
  - Transportes Aéreos Portugueses S.A. (TAP, S.A.).
  - TAPGER–Sociedade de Gestão e Serviços, S.A. e empresas subsidiárias:
    - CATERINGPOR–Catering de Portugal, S.A.
    - L.F.P.–Lojas Franca s de Portugal, S.A.
    - U.C.S.–Cuidados Integrados de Saúde, S.A.
    - MEGASIS–Sociedade de Serviços e Engenharia Informática, S.A.
  - PORTUGÁLIA–Companhia Portuguesa de Transportes Aéreos, S.A. (PORTUGÁLIA)
  - AEROPAR Participações, S.A. (AEROPAR) e empresa subsidiária:
    - TAP–Manutenção e Engenharia Brasil, S.A. (ex-VEM)

Subsidiaries are all the entities over which the Group considers there is control. It should be noted that the company L.F.P.-Lojas Francas de Portugal, S.A. was classified on December 31st, 2016 as a discontinued operation.

The following entity was classified as an associate:
// SPdH–Serviços Portugueses de Handling, S.A. (SPdH)

Aggregate performance of the companies of the TAP holding (Consolidation)

The attached consolidated financial statements of the Group were prepared in conformity with the International Financial Reporting Standards adopted by the European Union (IFRS – formerly called the International Accounting Standards – IAS) issued by the International Accounting Standards Board (IASB) and Interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) or by the former Standing Interpretations Committee (SIC), in force on the date of preparation of the said financial statements.

Presented below are the most important aspects of the overall performance of the TAP holding in 2016 and of each of the companies that constitute the core business in which the Company holds investments.

In 2016, two aircrafts were added to the TAP, S.A. fleet, namely two A330 for long-haul equipment. The regional fleet underwent significant structural changes, involving its full replacement by more efficient aircrafts, with eight ATR72-600 and nine E190. This structural change in the flight equipment allowed the Lisbon-Oporto Air-Shuttle connection to be launched, at the end of March, as well as new destinations to be opened, with flights to the JFK (New York) and Logan (Boston) airports in the USA and to Vigo in Spain. Flights to Guiné-Bissau were also reinstated at the end of the year.

Despite continuing to be negative, the result presented by the Group showed a significant improvement, but it is still greatly affected by a strongly unfavourable situation in some of the Company's main long-haul markets, which are traditionally more profitable.

Particular reference should be made to the impact of the continuous economic recession in Brazil, the contraction of the Angolan economy since the sustained decrease of oil prices, and the continued deterioration of the Venezuelan economy.

This way, TAP SGPS ended 2016 with a net profit in the amount of EUR -27.7 million, which represents a relief of EUR 128.3 million in relation to the EUR -156.0 million registered in 2015.

At the operational level (before finance and tax expenses), the Company registered a positive profit in the amount of EUR 13.0 million, reflecting an improvement of EUR 130.4 million, compared to the amount verified the previous year.

Profit before tax totalled EUR -28.3 million, a value which represents a relief of EUR 152.3 million regarding the EUR -180.6 million registered in 2015.

As for Air Transport, worldwide a total of 11.697 million passengers were transported, which shows a 3.3% growth compared to the previous year; however, a contraction of around 5.2% in 2016 as compared to 2015 in income from sales and services rendered should be noted.

This result was greatly affected by the erosion observed in the yield, as well as in the demand of certain traditionally more profitable markets. The most relevant case regarding long-haul activity is Brazil, as a result of a particularly unfavourable economic environment, and as for medium-haul flights it is Europe, a region with high competitive exposure.

It should also be noted that the activity of TAP–Maintenance and Engineering Portugal registered a total of EUR 78.0 million in income generated by sales and maintenance services rendered to Third Parties, which is 23.0% less than in 2015, because of the lower aircraft maintenance activity, thanks to the lack of available slots for third parties due to the programmes launched for the TAP fleet – sharklets and passenger cabin retrofit. In the engine business, there was a growth in comparison to 2015, following the strong commercial activity developed, and the component business remained relatively stable, thanks to the fleet management contracts held by TAP.

With respect to TAP S.A., the company registered a net profit of EUR 33.5 million, a value that is EUR 132.5 million higher than the -99.0 million registered in 2015. Operating profit reached EUR 24.0 million, that is, EUR 132.8 million more than in 2015, with net financial results in the amount of EUR 13.4 million, corresponding to an improvement of around EUR 24.4 million compared to the previous year.

As for Maintenance and Engineering Brazil Unit, TAP–Maintenance and Engineering Brazil continued to consolidate its operational and economic results. Economically speaking, reference should be made to a growth in sales of about 25%, in comparison to 2015, the budget having been exceeded for the first time. Despite remaining negative, and representing more than half the interest payment to Lisbon, the net profit showed a 20.6% improvement in relation to 2015. A strengthening of the contractual relations with other Brazilian Operators was also registered, and Azul, Air Transat (Canada) and TAP continue to account for more than half the turnover of TAP−Maintenance and Engineering Brazil. From the operational point of view, there was a very positive evolution in Rio de Janeiro’s base activity, with positive developments, generally speaking, in all Business Units except Engines, the performance of the latter deriving from the natural cycle of removals of the main Customer, Azul. Finally, with the return of the Operations Vice-President to Portugal, a new model of responsibilities was established, giving each Operations Base (Rio de Janeiro and Porto Alegre) its own person in charge and extinguishing the position of Operations Vice-President.

Contribution of associated companies

In terms of SPDH−Serviços Portugueses de Handling, S.A. (Groundforce Portugal), established in 2003 with the demerger of the Ground Handling Business Unit of TAP S.A., TAP, SGPS, S.A. holds a number of shares representing 49.9% of the respective share capital, a figure that includes a 6% stake held by PORTUGÁLIA−Companhia Portuguesa de Transportes Aéreos S.A.. In 2016, the company reached a positive net result of EUR 6.1 million, higher than the result of EUR 1.3 million reached in 2015.

Main Indicators

TAP, SGPS, S.A.
(Consolidation)

	2016 EUR million	2015 Reexpressed EUR million	var.
Operating Income/(loss) (earnings before interests and taxes)	13.0	(117.3)	111.1%
Pre-tax Earnings	(28.3)	(180.6)	84.3%
Net Income attributable to the shareholders of TAP SGPS	(27.7)	(156.0)	82.2%
Net Income of TAP, S.A.	33.5	(99.0)	133.9%
Net Income of SPdH–Serviços Portugueses de Handling, S.A.	6.1	1.3	375.7%
Net Income of Aeropar Participações, S.A. (Brazil)	(15.6)	(19.1)	18.4%
Net Income of TAP–Maintenance and Engineering Brazil, S.A.	(31.9)	(40.2)	20.6%
Total Assets	1,657.1	1,374.0	20.6%
Total Equity (after non-controling interests)	(469.6)	(530.3)	11.4%
Active Staff of the Group (31st December)	13,361	13,102	259
TAP, S.A.*	7,385	7,284	101
Air Transport	4,994	4,914	80
Loyalty	22	19	3
Maintenance and Engineering	1,911	1,911	0
TAP Serviços	423	409	14
Other	35	31	4
SPdH - Serviços Portugueses de Handling, S.A.**	2,303	2,172	131
Remaining Companies ***	3,673	3,646	27

(*) Not including staff who are not placed and not active
(**) Associated Company
(***) TAP –Maintenance and Engineering Brazil does not include trainees

Highlights

Structuring Events

During 2016, the Company increased efforts to guarantee a competitive position in the global market, particularly by promoting a transformation process that will allow it to reach and sustain high levels of operational efficiency and agility. The continuation of the occurrence of structuring events was also registered, among them the development of the Re-privatization Process, launched at the end of 2014. The main facts that took place in 2016 regarding this process are the following:

Timeline of the main events in the scope of the Re-privatization Process

06 February – Memorandum of understanding between the Portuguese Republic and Atlantic Gateway, with the purpose of setting out the principles and rules that the reconfiguration of the Portuguese State's participation in TAP SGPS should comply with, namely, the purchase of shares representing TAP's share capital by the Portuguese State, TAP's corporate governance rules, and TAP shareholders' economic rights.

19 February – Notification of ANAC's (National Civil Aviation Authority) **decision to TAP**, regarding the privatization process, setting certain constraints on management actions for a 90-day period, and whose implications were the object of analysis by TAP in the meantime.

8 March – In the General Assembly meeting of TAP SGPS S.A., the shareholders of TAP SGPS S.A., Atlantic Gateway and Parpública approved the issue, by TAP SGPS S.A., of EUR 120 million in bonds convertible in company shares, this issue being composed of two series: the first (series A), in the amount of EUR 90 million, subscribed by Azul, S.A.; and the second (series B), in the amount of EUR 30 million, to be subscribed until 20 June 2016 by Parpública or by Azul, S.A., if Parpública decides not to exercise its subscription right. The conversion of the above mentioned bonds into TAP SGPS shares, and the provision of guarantees regarding this issue, shall be subject to the express approval of ANAC.

19 May – Signing of the agreement between the Portuguese Republic and Atlantic Gateway, private shareholder of TAP, thus fulfilling the Memorandum of Understanding, concluded on 6 February 2016, which defines the conditions for the purchase by the Portuguese State of TAP SGPS shares, its rules of corporate governance, and TAP SGPS shareholders' economic rights. The conclusion of this agreement provides the clarification of the Company's situation, allowing TAP to concentrate its efforts on the execution of the TAP Group's strategic project, guaranteeing its development and the construction of a stronger company that is healthier from an economic and financial standpoint, a benchmark on a global level, more efficient, sustainable and competitive.

23 December – ANAC's approval regarding the decision on TAP's re-privatization, informing that: "TAP's and PGA's control structure, deriving from the purchase by Atlantic Gateway, is in accordance with what is laid down in Regulation (EC) no. 1008/2008, of 24.9.2008, which requires companies licensed to carry out Community air transport to belong to and be effectively controlled by Member States and/or nationals of Member States", and that "with this decision, the protective measures imposed by ANAC on 19.02.2016 are no longer in effect".

Main Events

February

After being introduced in Portugal, the Virtual Assistant – Sofia – is launched on the site www.flytap.com of Brazil and the United Kingdom, aiming to add real-time assistance to the existing communication channels, thus providing Customers with better quality online communication.

TAP is the first European company to introduce sharklet technology in its medium-haul fleet, with the completion of the installation on airplane A320, the first of its fleet to benefit from this alteration. This intervention, which improves operation with efficiency gains and emission reduction, was fully carried out at TAP's Maintenance and Engineering shops in Lisbon.

March

TAP joins the Lisbon Tourism Fair (BTL) and supports travel and tourism operators and agents from around the world coming to Portugal, so as to promote Portuguese tourist destinations and tourism businesses in Portuguese. At that time, the public is introduced at its stand to the Executive chairs equipping the two new A330-200 which reinforce its long-haul fleet.

TAP's on-board reading service – Digital Kiosk –, which offers offline reading of newspapers and magazines on personal mobile devices, is now also available in Windows Phone and Windows 8 operative systems.

Portugália and SPAC–Civil Aviation Pilots' Union sign an Agreement of principles and commitments for the transition of the Embraer E190 fleet in Portugália, representing a significant step in their mutual understanding of the importance and need to make the transition to the new airplanes, replacing the previous aircrafts Fokker 100 and ERJ145.

TAP creates TAP EXPRESS, which replaces the brand PGA–Portugália, with a new fleet and the provision of the Air-Shuttle PORTO/LISBON, thus investing in improved service, greater TAP brand and product consistency and reinforcing its commercial identity.

TAP commemorates the entrance of 90 aircraft Maintenance Technicians, with a ceremony during which their respective diplomas were handed out.

May

TAP's first Embraer 190 – of a fleet of nine E190 and eight ATR 72 –, operates the Company's regional network, with the colours of TAP Express, its entry into service being part of the renovation strategy of TAP's regional fleet.

June

To signal World Children's Day, TAP offered the first flying experience to 26 children and teenagers who take their flight baptism on the TAP's Air-Shuttle between Porto and Lisbon.

The partnership between TAP Portugal and Azul Brazilian Airlines began, as part of their respective frequent flyer programmes – Tudo Azul and Victoria –, allowing Customers of both companies to accumulate or use their points or miles when flying with the partner company.

Launching the expansion plan in the important North-American market, daily flights begin to Boston (USA) – Logan International Airport, with the new airplanes Airbus A330-200, thus adding the presence of one more American city besides Newark and Miami, and increasing the provision of direct flights between the two countries.

July

With daily direct flights between Lisbon and Vigo, the number of Spanish cities served by TAP rises to nine, thus joining Madrid, Barcelona, Seville, Malaga, Bilbao, Valencia, Oviedo and Coruña.

Daily direct flights are operated to Lisbon from New York – John F. Kennedy International Airport, with the new airplanes Airbus A330-200.

The programme *Portugal Stopover* is launched, encouraging long-haul passengers from the United States or Brazil to a final destination in Europe or Africa, with a stopover in Lisbon or Oporto, to enjoy their passage through Portugal and discover and visit the country, by staying up to three days in either one of those cities.

It is now possible, both in airports and on board, to upgrade to Executive Class, through fixed values created for this purpose.

August

Access to the boarding card is provided through Google Now, representing an evolution in the services TAP has come to offer its Customers on mobile devices, namely bookings and check-in, information about flight schedules, dissemination about prevailing price campaigns, and so on.

An additional functionality is included in the set of TAP's auxiliary services, making it possible to guarantee the favourite seat on board: a standard seat; in the first rows of the plane; a seat with more leg room, or a seat next to family or friends on the same flight. This service, which can be activated at any moment after completing the booking, through one of TAP's several sales channels, regardless of the purchased fare, is facilitated on all flights operated by TAP except for the Air-Shuttle service between Porto and Lisbon.

September

A new, more agile and dynamic commercial policy is implemented, involving the offer of the most competitive market prices for destinations in Europe and in North Africa (Algeria and Morocco). In this manner, the Company now competes in the lower-fare segment of the market and it is up to the Customer to choose, in a simple and transparent way, the service level best suited to the trip in question, exclusively for the price corresponding to the type of product valued.

October

The NPS, the metrics with which Passengers' satisfaction level can be measured, is launched, allowing the Company to hear its Customers about the different moments of their TAP experience – before, during and after the flight –, and to promote specific actions to better target their products and services.

By pursuing an innovation policy, TAP is among the first airlines in Europe to allow Passengers to acquire one way only fares for intercontinental flights, by making these fares available with a simple pricing structure and competitive prices.

November

The new online sales platform is launched on https://flights.flytap.com, a new digital tool which optimises the Customer's search for flights, showing the lowest prices for any TAP destination and allowing an immediate booking online.

Following the interest the public displayed in the A330neo cockpit replica at the Web Summit, TAP's airplane of the future is exhibited at Lisbon Airport, for a period of time covering the Christmas season.

The working agenda of IBE Agile Team – a multidisciplinary team established with the purpose of designing the new booking engine of TAP's site – begins. The new FlyTAP marks a new relationship with Customers, following the strategy defined by *New TAP*, directed at listening to the real needs of its Passengers. Among the various innovations made available, such as travel search according to the user's budget, by registering in the new Customer Area, Customers will be allowed to personally manage their profile online, access their bookings, do upgrades and also acquire *additional services*.

December

Flight operations to Guinea-Bissau are resumed, reinforcing TAP's position in Africa, a continent considered to be one of its strategic markets.

Continuing its investment in innovation and following the trends and current patterns of communication, the app TAP FlyMoji, a pioneer for smartphones, is made available to exchange messages.

Distinctions and Prizes awarded in 2016

Continued strengthening of prestige in the markets in which the Company operates:

- Impact on the economy, recognition in various regions of the world;
- The dissemination of the culture, values and products, in a partnership of national scope;
- Promotion of contributions witnessing concerns related to human rights.

Europe

Magazine UP Leader in Europe – Trophy awarded to TAP's inflight magazine, at the World Travel Awards (WTA) – the Oscars of world tourism.

Tourism Multimedia Award (Economy category) – Special mention to TAP's *Safety Video* – which is a homage to Lisbon, besides divulging safety instructions aboard airplanes –, at the 14th edition of the *Golden City Gate* Awards (*Das Goldene Stadttor 2016* " – *Tourism Multimedia Award*") during the Berlin ITB, one of the largest Tourism fairs worldwide.

Alentejo and Ribatejo Tourism Awards (Communication Trophy) – Award given to UP magazine at the 6th edition of the Alentejo and Ribatejo Tourism Awards, for the number where this Portuguese region is highlighted, thus contributing to the affirmation of these destinations in the national and international markets.

First Airbus A330neo operator with Airspace cabin – Signing of an agreement between TAP and Airbus, during the AIX – Aircraft Interiors Expo 2016 (Hamburg), through which the Company becomes the first operator of the new A330neo airplane equipped with the new version of the Airspace by Airbus cabin, which will integrate a 14-craft fleet from the end of 2017 onwards.

Travel Plus Awards 2015 Golden Award (Ethically Sustainable Amenity category) – Award given to TAP's Executive Class on-board kits, with an original design inspired by the traditional Portuguese sardine cans, whose materials reflect ecological and sustainability concerns.

TAP in the Top 20 of the most attractive companies to work in Portugal – TAP's position identified during the Randstad Award, a study undertaken by this Human Resources company, developed by the ICMA Group, which assesses companies' attractiveness according to the active population's perception.

Creativity Prize (Digital and Interactive Media category – Best Motion Graphic) – Within the 18th Festival of the Portuguese Creative Club 2016, distinction awarded to TAP Maintenance and Engineering's (TAP M&E) commercial film, which aimed to innovatively and uniquely present and promote the services offered by TAP M&E in the global market of MRO (Maintenance Repair and Overhaul).

Best Airline Company (Airline Companies category) – Distinction awarded to TAP on the occasion of the Marketeer trophies, which distinguish performances in the fields of Marketing, Publicity and Communication in Portugal, thus reflecting the reputation and prestige recognition of the TAP brand in Portugal.

TAP in the TOP 10 best airlines in the world – Position awarded to TAP, by eDreams customers, as the 9th best airline in the world in 2016, reflecting an upward trend compared to the previous year.

Africa

Leading European Airline to Africa – Award given to TAP at the World Travel Awards (WTA) – the Oscars of world tourism –, in recognition of its ongoing effort, in pursuance of excellence, by promoting the best product in Europe-Africa connections.

United States of America

Fourth *Most Loved* airline in the world on the social media – TAP's position according to a survey carried out in the United States of America and published in Fortune magazine, which analysed 1.3 million tweets, involving 70 airline companies around the world, during the Christmas peak travelling period, considered to be the most stressful period of the year to travel.

Gold Medal at New York Festival's World's Best TV & Films (Sales category) – Distinction awarded to TAP's Safety Video which is a homage to Lisbon, besides divulging safety instructions aboard airplanes –, during the edition of this North-American film festival (Las Vegas), devoted to the TV and film industry.

Best Wines Served on Board – Rankings attributed, as 1st best and 2nd best, among the best wines served in the main airline companies worldwide, by the North-American magazine Global Traveler, to two of the Portuguese wines served by TAP in executive class – *Paulo Laureano Reserva* 2014 (Best International Business Class White Wine) and Churchill´s Estates *Grande Reserva* 2011 (Best International Business Class Red White) –, confirming the quality of our national wines.

Best City and Best Airline Company for Stopovers in Connecting Flights – Rating given by the global reference North-American magazine Condé Nast Traveler, to Lisbon and to TAP, just three months into TAP's Portugal Stopover programme.

Highlight on North-American TV channel – Distinction awarded to TAP's Portugal Stopover, on a large-audience show of the North-American TV channel CBS.

Best European Company and Best New Route Launch – Rankings attributed by the North-American magazine Global Traveler to TAP and to the Boston-Lisbon route launched by TAP in 2016.

South America

Leading European Airline to South America – Award given to TAP at the World Travel Awards (WTA) – the Oscars of world tourism –, in recognition of its ongoing effort, in pursuance of excellence, by promoting the best product in Europe-South America connections.

Second best loyalty programme in Brazil – Ranking attributed to TAP's Victoria Programme, by the Brazilian site *Melhores Destinos* (http://www.melhoresdestinos.com.br/), following a survey about the best international miles programmes.

Corporate Strategy

Srategic Plan 2015-2020
Strategic Axes

1. Renewal and expansion of all the fleets;
2. Evolution of the commercial model;
3. Automation and improvement of the Customer experience;
4. Consolidation of the Company's growth and increased focus on the hub;
5. Operating efficiency improvement;
6. Repositioning of the maintenance and engineering business units in Portugal and in Brazil.

Implementation of the strategic axes defined for TAP at the end of 2015 resulting from the privatization process

The sequence of a set of factors, of external and internal nature made evident the need to rethink the long-term strategy for TAP: In particular: i) the large number of non-recurring events and the reduction of the yield experienced, with a direct effect on the Company's profitability; ii) the level of underinvestment felt and the impact on the fleet and quality of the product; iii) the need to keep up with peers in their efforts to cut costs, which could jeopardise the cost advantage that currently benefits TAP; and iv) the need to adapt TAP's commercial model to a new reality in the Industry.

To that effect, at the end of 2014, a strategic reflection was initiated for the 2015-20 period, and six strategic axes were defined as a guide for the Company to establish itself in the world market as a growth reference and to consequently increase its representativeness in the markets in which it operates and will operate as well as in the general context of the aviation industry.

A new strategy for the Company as from early 2016

Meanwhile, the year 2015 was marked by the TAP reprivatisation process and consequently by all the efforts undertaken internally in this sense. This process underwent several stages and started in late 2014. In January 2015, the specifications of the operation regarding the privatisation of the Company were published in the *Diário da República* (Government Gazette). In May 2015, three groups of interested investors submitted their final and binding offers to the Government and in June 2015, the final decision of the Portuguese Government was publicly announced. The process was effectively concluded on 12 November 2015 through the sale of shares representing 61% of the share capital of TAP SGPS to the Atlantic Gateway consortium in the form of a reference direct sale.

Throughout 2016, the development of a series of structuring actions continued, aimed at enabling the implementation of TAP Group's strategic project, in the sense of ensuring its development and the construction of a stronger company that is economically and financially healthy and a worldwide reference. Thus, as part of the second phase of the re-privatisation process, in February 2016 a Memorandum of Understanding was concluded between the Portuguese Republic and Atlantic Gateway, with the purpose of setting out the principles and rules that the reconfiguration of the Portuguese State's participation in TAP SGPS should comply with, namely, the purchase of shares representing TAP's share capital by the Portuguese State. The implementation of the Memorandum of Understanding would take place in May 2016, with the signing of the agreement between the Portuguese Republic and Atlantic Gateway, private shareholder of TAP, the conclusion of which brought clarification to the Company's situation and allowed efforts to concentrate on giving the organisation better levels of efficiency, sustainability and competitiveness.

In this regard, in July 2016 a Notification regarding the launch of the project TAP's Transformation Process was carried out, aimed at continuing the transformation effort conducted in this Company, in recent years, in a structured manner and in line with international best practices. Meanwhile, in December 2016, ANAC's decision regarding TAP's re-privatization was issued, informing that TAP's and PGA's control structure, deriving from the purchase by Atlantic Gateway, is in accordance with what is laid down in Regulation (EC) no. 1008/2008, of 24.9.2008, which requires companies licensed to carry out Community air transport to belong to and be effectively controlled by Member States and/or nationals of Member States, and that, with this decision, the protective measures imposed by this Authority on 19.02.2016 are no longer in effect.

The design of a new Company strategy thus emerges, the implementation of which began at the start of 2016 and included changes in the Fleet, Network, Product and Capitalization Plan.

In this context, Atlantic Gateway provided supplementary benefits to TAP SGPS, amounting to around EUR 154 million, immediately following the reprivatisation. This inflow of funds helped to increase liquidity and was used to recapitalise the TAP Group, in particular the company TAP, S.A..

At the time of privatisation, the Atlantic Gateway consortium reaffirmed the following commitments made during the process:

- Complying with public service obligations;
- Maintaining the integrity, corporate identity and autonomy of the TAP Group;
- Preserving the TAP brand and its association with Portugal, ensuring that its headquarters remain in the Country;
- Maintaining and reinforcing the hub in Lisbon;
- Contributing to the development of the national economy;
- Entering into commitments with regard to labour stability and developing and making the best use of human resources.

Meanwhile, the economic crisis in Brazil and in Angola represented the factor with the most significant negative impact in TAP's main long-haul markets, traditionally more profitable. It is also worth mentioning the growing competition in Europe.

In this context, the Strategic Plan announced in late 2014 (**Strategic Plan 2015-2020**) has consequently suffered, at the end of 2015 and in the course of 2016, changes in the main strategic axes, namely:

Renovation and expansion of all fleets – The renewal and expansion plan remains standing and includes 53 new aircraft, 14 Airbus 330-900 Neo for long-haul flights (in replacement of the A350 aircraft), and 39 Airbus A320 Neo aircraft for the medium-haul. In addition, a reinforcement of the fleet of TAP, S.A. – 3 airplanes, namely 2 aircraft of A321 and A320 models, in the narrow-body fleet and 1 A330 aircraft, which will complement the existing wide-body fleet – will allow the opening of new routes, as well as the increase of frequencies for some destinations, in 2017.

Concerning the regional fleet, mention should be made of the replacement, in 2016, of the former fleet of Portugália with newer and more efficient aircraft, in terms of fuel consumption, allowing the new aircraft operated under the TAP Express brand to increase the competitiveness of the fleet. In particular:

- Nine E190 regional aircraft for Portugália;
- Eight ATR 72-600 turbo-prop aircraft for TAP, S.A., under an ACMI agreement with White Airways.

Consolidation of the Company's growth and increased focus on the hub – The growth of the network focused on hub and the consolidation of growth in Brazil continue to be the main objectives. The expansion of the long-haul network implies new strategic markets and the Lisbon-Oporto Air-Shuttle closes some markets from Porto. The priority is focused on rebuilding the company's profitability in order to secure its financial future, which justifies the need to adapt and optimise routes and capacity. The new Exploration Plan, which will ensure the future of TAP, S.A., requires that changes be made to the network and capacity that will significantly improve the Company's economic and financial performance. The main long-term strategies of the network are to:

- **Building and reinforcement of the Lisbon hub**
  - ⇨ Improving the consistency of schedules;
  - ⇨ Improving connections;
  - ⇨ Increasing the offer of long-haul services so as to increase the value of the hub, simultaneously reducing the single-country risk;
  - ⇨ Improving reliability through the operation of a consistent schedule.
- **Launch the Lisbon-Oporto Air-Shuttle in March 2016, with a high-frequency shuttle service**
  - ⇨ New flights every hour between Lisbon and Oporto at competitive prices;
  - ⇨ New aircraft and new products designed to improve customer experience, particularly at airports.

- **Active management of network capacity so as to optimise results**, with an initial bet in 2016 on increasing the number of flights to North America and the number of connections in Brazil.

Axis of automation and improved customer experience – The focus remains on the intention to improve the on-board experience through the investment in state-of-the-art cabins in wide-body and narrow-body aircraft.

A strategic vision for the future

TAP SGPS has a strategic vision for the future and one of the key objectives is to create a financially sustainable airline.

Highlights of the Strategy for 2016-2017

- In the context of the acquisition by Atlantic Gateway of 61% of the share capital of TAP SGPS, the sole shareholder of TAP, S.A., the consortium reaffirmed its determination to urgently implement the recapitalisation process of TAP SGPS, of TAP, S.A. and of other subsidiaries, immediately resolving the most pressing problems by reinforcing the company's financial capacity. In this sense, it was considered an investment (the Capitalization Amount), with the following breakdown, whose realization was fully implemented:
  - ⇨ EUR 154.4 million on 12 November 2015 for supplementary benefits, already invested in TAP, S.A.;
  - ⇨ EUR 120 million before June 2016, in guaranteed 10-year convertible bonds with no cash interest, amount (EUR 50 million) partially invested in TAP, S.A., through the reduction of financing granted by TAP, S.A. to TAP SGPS;
  - ⇨ EUR 69.7 million in 2016 of supplementary benefits, amount invested in TAP, S.A. through the reduction of financing granted by TAP, S.A. to TAP SGPS.
- The creation of a new brand: TAP express – With this brand, the TAP Group aims to serve regional and domestic routes, using the new Embraer E190 fleet (operated by Portugália) and ATR72-600 aircraft (operated by White Airways) and replacing the commercial name Portugália (PGA Airlines), reflecting the offer in 2016, an increase in seats offered, in the order of 50% compared to the previous year;
- Continuing the commitment of the TAP Group to serve Portugal and Portuguese-speaking countries:
  - ⇨ Maintaining the market leadership for Brazil – European capacity;
  - ⇨ Despite the economic downturn, continuing with the service to Angola and Venezuela, considered important destinations for the Portuguese diaspora;
  - ⇨ Exploring new routes to Portuguese communities in the United States, aimed at growing in 2016 and 2017;
  - ⇨ Continuing to operate all domestic routes and increasing the capacity between Oporto and Lisbon.
- Changes in the fleet with the goal of positioning TAP among the best Airlines in the world and granting an increasingly decisive role in connections between Europe, Africa, Brazil and North America:
  - ⇨ New Fleet – The investment plan includes an order for 53 new aircraft (14 Airbus 330-900 Neo and 39 Airbus A320 Neo family) whose delivery will begin during the 1st and 3rd quarter of 2018, respectively. The underlying objective is the reduction in cost per passenger as these new aircraft are cheaper and more efficient for long-haul flights, which involve a larger investment;
  - ⇨ Revamping the fleet – In addition to acquiring new Airbuses, TAP will revamp the medium- and long-haul fleet in an operation that will, mainly, be carried out, in TAP's Maintenance and Engineering workshops. Around EUR 60 million have already been allotted to the reconfiguration of 41 medium-haul aircraft with the aim of improving the comfort of passengers, increasing the quality and competitiveness of the product;
  - ⇨ Integration, in 2017, of 7 additional aircraft, including 3 Airbus aircraft in TAP, S.A. and 4 E195 in PGA, under operating leasing, as previously mentioned;
  - ⇨ Renewing the Portugália fleet – Providing a 51% increase in 2017, compared to 2015, in the number of seats available and 40% savings in fuel consumption, with the consequent advantages for the environment;
  - ⇨ Introducing Sharklet technology in some aircrafts of the medium-haul fleet – The application of these devices, begun in 2016 and terminus planned for early 2018, will provide improved aerodynamics of the aircraft, resulting in lower (on the order of 2.5%) fuel consumption, less emissions and extending the operational life of the aircraft.

Key developments in 2016 under the 2015-2020 Strategic Plan

Within the framework of the six strategic areas of the Strategic Plan for the 2015-20 period the following developments deserve special mention.

First axis of renewal and expansion of all the fleets – 2016 was a transitional year during which several projects, which were already under way in 2015, were implemented. Other projects are expected to be implemented over the coming years. In the TAP fleet, which at the end of the year totaled 63 aircraft (43 medium-haul and 20 long-haul), most of the changes concerned the cabin interiors, with a view to expand the number of seats while maintaining, or even increasing, the level of comfort in the case of the medium-haul fleet. In the TAP long-haul fleet, two A330-200 were added.

In the regional fleet, there were significant structural changes involving its full replacement. The brand TAP Express was created and applied to the entire operation in this regard, ensuring brand consistency across the airplanes operated by TAP. The old regional fleet was progressively replaced throughout 2016 with 8 aircraft of model ATR72-600 (with 70 seats), under ACMI regime, operated by White Airways (discontinuing the use of the ATR42-600), and by 9 aircraft of model E190 (with 106 seats), more recent and more efficient in terms of fuel consumption, whose operation is run by Portugália. The ATR aircraft were predominantly for use in the Lisbon-Oporto Air-Shuttle, which began at the end of March.

Second axis of evolution of the business model – The Company’s business model has evolved, providing customers with more options and creating new products and services, in addition to the trip. It can be considered as the beginning of a Customer Choice model, with development in 2016 and subsequent years, with customers defining the services and benefits associated with the respective commercial rate. An extensive Ancillary Services program was launched, available in both the company’s direct and indirect distribution channels, offering customers a variety of products.

The Victoria Program – TAP's Loyalty Program maintained the autonomy within the company TAP, S.A., preserving transparency criteria regarding the performance of this activity in an autonomous way.

Concerning a third axis of automation and improvement of customer experience – TAP’s new strategy has focused on the Customer, improving and optimizing its products and services, modernizing the fleet and on-board comfort. In line with this, in 2016 a series of initiatives were launched, namely the NPS (Net Promoter Score), which aims to promote broader knowledge about Customers’ level of satisfaction, and identify which points eventually reduce this level, thus enabling a rapid, targeted intervention; the Project Flying for Gold, aimed at improving the Gold Customer’s experience, by supporting the improvement of service quality and the resolution of irregularities, rewarding loyalty, improving and modernizing communication; the creation of a Concierge service for higher-value customers. There is an outreach initiative called Listening to the Customer, which put elements of TAP’s Management and Board of Directors in touch with its most frequent customers, to actively listen to their main remarks, opinions and suggestions about the Company, and to act directly upon this feedback.

Aimed at improving Customer experience, the launch of Portugal Stopover should also be mentioned. This project encourages long-distance passengers from the USA or Brazil, and whose final destination is Europe or Africa, to pass through Portugal and enjoy the visit to the Country, staying up to 3 days in any of the cities where they stop over – Lisbon or Oporto.

On the other hand, the new online sales platform was launched on https://flights.flytap.com, a new digital tool which optimises the Customer’s search for flights, showing the lowest prices for any TAP destination and allowing an immediate booking online. Also, IBE Agile Team, a multidisciplinary team, is established with the purpose of designing the new booking engine of TAP’s site. The new FlyTAP is developed following the strategy defined by the New TAP, directed at listening to the real needs of its Passengers. Among the various innovations made available, such as travel search according to the user’s budget, by registering in the new Customer Area, Customers will be allowed to personally manage their profile online, access their bookings, do upgrades and also acquire additional services.

Regarding on-board comfort, the two A330-200 which integrated the TAP fleet in 2016, preferentially operating on the two new routes of the US market (New York JFK and Boston), translated into a significant improvement of the product offered to passengers and represented the launch, in advance, of the type of cabin product TAP intends to offer its passengers in the future and which will be extended to the rest of the fleet.

Following the conclusion of the privatisation process and above all in 2016, the definition of the new A330neo, of which TAP will be the first operator, took place. This process aimed to define a product in line with the needs of passengers, focusing on greater comfort, innovation in terms of the entertainment and connectivity system, and an alignment to the new image of TAP’s cabin interiors. After the first delivery, scheduled in March 2018, the older A330 will begin to be removed, as well as the A340 equipment. A programme to modify A320fam cabins, of a series of 41 airplanes of the medium-haul fleet, is also under development, the first modification having taken place in November, with a predicted conclusion at the end of 2017. The renovation programme of cabin interiors of 7 A330, used in long-haul flights, will also be carried out in 2017. This cabin modification brings about a redefinition of the offer to passengers, improving the levels of comfort by installing new chairs and increasing the number of seats on board so as to align with the product of the most direct European competitors; it also allows quite a significant reduction of the airplanes' weight and, inherently, a reduction in fuel consumption. In this programme, TAP reinforced its investment in the national economy by choosing national partners to create the product, including the design of the chairs, the supply of materials (leather) and the production of covers for the chairs. All these interventions will be executed mainly in the aircraft maintenance workshops owned by the TAP Group in Portugal and in Brazil.

Fourth axis of consolidation of the Company's growth and increased focus on the hub – In 2016, the Company remained strategically focused on improving the network by strengthening the Lisbon hub through the potential increase in traffic between Europe and TAP destinations in North and South America and Africa. Two new destinations in North America were introduced, namely New York (JFK) and Boston, having started in Europe direct direct connections between Lisbon and Vigo, in Summer 2016. In Africa, the operation of flights to Guinea-Bissau was resumed, reinforcing the Company's position on this continent, considered as one of the Company's strategic markets.

The main goal was to develop existing markets or to conquer new opportunities in markets as yet unexplored, with operations in Funchal and Oporto remaining unchanged, in accordance with the performance registered.

Fifth axis of improvement in operational efficiency – According to plan, in 2016 the project TAP's Transformation Process was launched. This initiative was developed to continue the Company's transformation effort in a structured manner and in line with international best practice as regards operational efficacy, efficiency and agility, but without compromising the Company's resolution to maintain excellence in the safety of its operations and to offer its customers a world reference product and service. In 2016, despite being under the effect of a gradual rise in fuel prices, a reduction in the unit operating cost was registered.

Sixth repositioning axis of the maintenance and engineering units business in Portugal and in Brazil – With regard to TAP–Maintenance and Engineering Portugal, although in 2016 there was a decrease of about 23% in sales to third parties (12% less if we consider the effect of variations in production), this did not happen because of a lower effort in sales or less competitiveness; rather, it was simply the result of the occupation of hangar slots, to comply with the modification programmes of TAP aircrafts – sharklets and changes in cabin interiors –, which prevented a greater turnover in terms of aircraft maintenance. In fact, there was growth in the engine maintenance business and stability in the turnover of components maintenance. Since the same trends continue in the MRO market and given the results obtained, the Company believes in continuing its current commercial strategy, based on market niches, but without neglecting greater opportunities, such as in the engine sector, where there is still plenty of capacity, and in the operational strategy which aims at providing Maintenance and Engineering with the technological capacity and processes which will ensure the efficiency and quality that are essential for the levels of competitiveness needed for their sustainability. It is in this context that the topic of Innovation and the implementation of a Culture of Innovation have been producing results.

TAP–Maintenance and Engineering Brazil continued converging towards operational balance. For the sixth year in a row, the company's activity grew again, about 25% in Reais, and for the first time it registered a sales amount higher than the budgeted figure (Reais 319 Million vs Reais 316 Million). As it will not be possible to maintain these growth rates in the medium term, in a market that grows around 6% per year, it was decided to take more aggressive measures leading to cost reduction, so as to accelerate convergence towards positive results. An organizational restructuring was also carried out, leading to the improvement of operational performance, and several activities continued as regards productive processes aimed at further efficiency.

The development of a methodology aimed at identifying opportunities and optimizing synergies with the airline company Azul should also be mentioned.

Other TAP Group Companies

With regard to the remaining participations held by TAP, SGPS, S.A., reference should be made to the development of the activity in areas related to the Group's core businesses – Air Transport and Maintenance and Engineering. The criteria for the selection of these investments was based on the assumption that the development of the respective activities contributes to strengthen those businesses, both by the return on invested capital and the increase in competitive advantages promoted by the synergistic effect. TAP has a company that operates as a holding for some of its subsidiaries which develops activities that are complementary or collateral to its core businesses of air transport and maintenance – TAPGER–Sociedade de Gestão e Serviços, S.A. – whose main objective is to monitor the management of those companies in a direct and participatory way.

In keeping with the trend in the Industry, TAP holds its financial investments in the areas of catering, information systems, sales in airport stores and on board, health services and ground force services.

Performance Analysis

TAPGER–Sociedade de Gestão e Serviços, S.A.

TAPGER is a public limited liability company based in Lisbon, created by TAP in September 1997 for the purpose of achieving more direct and active management of the various complementary or collateral activities of the core business of air transport and maintenance, with a view to its development. The company’s objective is the supervision of the management of its participated companies, particularly their respective financial and economic performance, as well as the provision of assistance and support to the companies Lojas Francas de Portugal S.A. and Cateringpor–Catering de Portugal, S.A., in specific areas, as established under the Joint Venture Agreement and Technical Service Agreement, respectively. In order to ensure this assistance and the entire administrative process in a more satisfactory manner, TAPGER maintains a service contract with TAP, S.A. (TAP Serviços).

During 2016, TAPGER monitored the activity developed by its participated companies and held the necessary general meetings for the approval of the respective accounts relative to the financial year of 2015.

The net income for the tax year of 2016 increased by 16.5% in comparison to 2015 (EUR 780.8 thousand more).

Other TAP Group share holdings, on 31st December, 2016

EUR thousand

		Stake of TAP	Amount of TAP Share Capital	Net Income
Portugália, S.A.		100%	15,000.0	(1,479)
Aeropar Participações, Lda. (Brazil)		100%	0.2	(15,621)
	TAP–Maintenance and Engineering Brazil, S.A	98.64%	207,057.7	(31,879)
TAPGER–Sociedade de Gestão e Serviços, S.A.		100%	2,500.0	5,518
Catering	Cateringpor-Catering de Portugal, S.A.	51%	1,785.0	1,549
Airport Shops and In-flight Sales	LFP–Lojas Francas de Portugal, S.A.	51%	280.5	8,944
Information Systems	Megasis-Soc. de Serv. e Eng. Inf., S.A.	100%	500.0	66
Health-Care Services	UCS–Cuidados Integrados de Saúde, S.A.	100%	500.0	52

Outlook for 2017

Macro environment and market conditions in the sector

Following a growth of around 3.1% in 2016, world economic activity is expected to continue climbing, with a slightly higher evolution predicted for 2017, at 3.4%, which is still lower than the pace observed before the crisis. However, the broad dispersion of possible results regarding the development of global activity should be noted, given the uncertainty of the political orientation of the new US Administration and its respective ramifications worldwide. The prospects between the advanced economies and the emerging and developing markets remain mixed, the behaviour of the latter deserving special attention.

Thus, activity in the United States is expected to continue being supported by further overall accommodative policies and by improving work markets, whereas in Japan the pace of expansion is expected to stay moderate. In the United Kingdom, growth perspectives should be limited by heightened uncertainty regarding the country's future relations with the EU. Additionally, it is probable that the current growth deceleration in China will negatively impact the economic perspectives of other emerging market economies, while in prospective terms the gradual slowdown of deep recessions in some of the main exporters of raw materials continues to be a source of support for worldwide growth.

As regards prices, following the OPEC agreement of last November oil prices have gone up, thus promoting a slow, progressive reduction of the effects of drops in oil prices, in the past, on global inflation worldwide.

In the euro zone, economic activity is expected to grow around 1.7%, the pillar of this evolution continuing to be internal demand, supported by the ongoing improvement of the work market and by improved bank financing conditions, reinforced by the ECB's significantly accommodative monetary policy stance.

In this regard, and based on the perspective of continued gradual recovery of the GDP and of a low level of inflation (1.3% in 2017, lower than the 2% reference), the ECB's decision last December to leave its key interest rates unchanged, and to prolong its asset purchase programme, which was intended to end in March 2017, should be noted. In keeping with the expected gradual recovery worldwide, exports are projected to progressively pick up, yielding an improvement of the contribution of net trade.

At the same time, a solid reinforcement of business investment is expected supported by companies' increasing confidence, by the level of capacity utilization, now at its highest since 2008, and by the outlook on demand developments. It is hoped that the government deficit ratio will decrease the level of 2016, reaching 1.6% of GDP.

As regards the Portuguese economy, after a 1.2 per cent growth in 2016, projections point to the maintenance of the trajectory of moderate recovery which has characterised recent years and which should result in a slight acceleration of the Gross Domestic Product (GDP) to 1.4%, in 2017 – a behaviour close to, but below, what the European Central Bank (ECB) projected for the euro area, without reversing the accumulated negative output gap between 2010 and 2013. Assuming a globally favourable external climate, though less than in previous years, regarding global trade flow, underlining this behaviour is export development which will continue to be the component of global demand which most contributes to the activity's growth, with exports of goods and services expected to register greater momentum than that of external demand, as observed in the last few years. The development expected for the Portuguese economy will also be sustained by an acceleration of the Gross Fixed Capital Formation (GFCF), based on the recovery of business investment. On the other hand and in keeping with the economic trends, private consumption is expected to decelerate regarding the behaviour observed in recent years; this is strongly related to the expenditure on durable consumer goods, partly deriving from the implementation of decisions delayed during the 2011-2013 recession. The development of the activity should be accompanied by the gradual recovery of the situation in the work market, with an expected continuation of job growth, though at a progressively more moderate pace. Inflation, as measured by the Harmonised Consumer Price Index (HCPI), should increase over the projection horizon, maintaining levels close to those projected for the euro area average. The continuation of reductions in the levels of indebtedness of the private sector is also expected and, based on the evolution of income and capital account balances, outside financing capacity is expected to be maintained, though lower than the capacity observed in the last few years.

As regards the Air Transport Sector, after having reached the best result ever in 2016, and despite the prospect of worse conditions surrounding it (particularly because of the rise in oil prices), in 2017 the Industry hopes to achieve an even stronger result globally, at around UD 29.8 billion, in comparison to the USD 35.6 billion estimated for 2016.

A reduction is therefore expected regarding stimulus on demand, which is associated with lower oil prices, motivating a slowdown in global growth, which should be around 5.1%, expressed in passenger kilometres utilized (PKU). The capacity growth in the sector is expected to reach 5.6%, overtaking the increase in demand, thus prompting a decrease in passenger global load factor to 79.8% (down from 80.5% in 2016).

However, this traffic behaviour will not extend to all regions, as lower developments are expected in more mature markets, such as Europe and the North Atlantic (4.0% and 2.5%, respectively). Weak performances are also predicted in the African region under the effect of regional conflicts and of the impact of low prices of commodities; and in Latin America where, despite some signs of improvement regarding the region's currencies and economic outlooks, operational conditions continue with a high potential for improvement, with poor infrastructures, high taxes and a growing regulatory overload all over the continent. Venezuela stands out in violation of the international obligations, continuing to block the repatriation of the Industry's funds.

Regarding air cargo transport, there is a certain optimism concerning cargo business perspectives for 2017, pointing to the interruption of the yield fall, and a moderate increase in demand (3.5%), though commercial conditions will continue to be challenging.

Outlook for TAP in 2017

Under the reprivatisation concluded on 12 November 2015, a number of changes were contemplated – including a Capitalisation Plan, already fully implemented, targeting TAP SGPS, S.A., TAP, S.A. and other subsidiaries. The Capitalisation Plan will indirectly strengthen the shareholder structure of TAP, S.A. and position it positively for future growth. The details of this strategy, in the year 2017, particularly as regards the Fleet, Network and Product, are given below.

Air Transport

Changes in the Fleet

During 2017, TAP is continuing its fleet and operating expansion effort, which began in 2016, with a reinforcement of equipment with two A320fam aircrafts and an aircraft of the A330 fleet. In the regional fleet, it is planned to continue the structural change begun in 2016, with the growth of the Portugália fleet from 9 to 13 aircrafts, due to the integration of 4 Embraer 195.

Key changes to the Network

The Exploitation Plan that will ensure the future of TAP, S.A. requires changes to the network and capacity, which will significantly improve the Company's financial performance. Worthy of mention are the main long-term network strategies, which will be implemented in the 2017 summer schedule: Building and strengthening the Lisbon hub; growth, in North America with the beginning of flights to Toronto, in Africa with the beginning of flights to Abidjan and the reinforcement of flights to Dakar and Marrakech. Additionally, new flights are expected to begin in Europe, with a view to diversify and expand the Company's portfolio, namely Las Palmas, Alicante, Cologne, Stuttgart, Budapest and Bucharest. As part of an ongoing management of routes and flight portfolio, an ongoing performance evaluation will be carried out on a continuous basis. Over time, the frequency will be adjusted to existing markets in accordance with changing economic conditions and new markets will be launched as soon as possible. Priority will be focused on restoring the company's profitability in order to secure its financial future, which justifies the need to cancel some routes and to reduce operations in certain markets in Lisbon and Porto.

The commitment of TAP, S.A. to Portugal

TAP, S.A. recognises that the long-term value of serving Portugal and the global Portuguese community currently outweighs the potential benefits of concentrating on the present development of the Lisbon hub. For this reason, the Company will keep some routes in Oporto during the summer schedule of 2017 through additional strengthening in Lisbon, which includes keeping certain long-haul routes to New York, Rio de Janeiro and Sao Paulo from Oporto, as these are important routes for the Portuguese diaspora and the business of local communities. Similarly, the Company will continue to fly to all Portuguese islands currently in operation.

In turn, the expected growth of TAP, S.A. in North America is intended to capitalise on an important and growing market like the US and to diversify the strategy of the significant capacity invested in Brazil. In this regard, the launch of the route to YYZ airport (Toronto) is expected on June 10th, 2017, with five weekly flights.

TAP, S.A. will continue with the long-term strategy of becoming the market leader in Europe in relation to the markets of Brazil, despite the fall in GDP and negative forecasts for the Brazilian economy. It will also continue to serve the Portuguese communities abroad, complying with service levels similar to those of the summer of 2016. The code-share service with the airline Azul Linhas Aéreas Brasileiras was authorised and started on December 10th, 2015. It is hoped that this will bring revenue improvements as well as connections for passengers between cities in Brazil and Europe.

Additional changes to the type of service

In complying with its full-service company mission, it is planned to continue, in 2017, the investment in TAP, S.A. in terms of equipping both wide-body and narrow-body aircraft with state-of-the-art cabins, with the aim of improving customer satisfaction and attracting new customers. The relaunch of this product started with the A330-200 fleet, with cabins refurbished to include new fully-flat seats in business class and video-on-demand and entertainment in both cabins, offering a superior experience onboard. It is anticipated that the entire A330-200 fleet will be renewed until the end of 2017. The program for the definition of the new A321neo Transatlantic, whose phase-in is expected to begin to occur during the year 2018, will be held during 2017. These aircraft, which will allow to explore some markets in North America, Brazil and Africa, will offer the passenger a comfort equivalent to that available in long-haul aircrafts, namely, a business class chair with a completely horizontal bed, greater spacing between economy class rows and an innovative entertainment and connectivity system.

In addition, the aircraft operated under the TAP Express brand, with modern cabins and a full-service product in line with the European experience of TAP, S.A., namely a special quality of service introduced in the Air-Shuttle, offering exceptional timing, recognizing the importance of speed to passengers on domestic trips.

Also, as part of the effort made by the Company to reflect an organization focused primarily on its Customer, to mention the creation of the Customer Committee, as a forum for the identification of priority actions to be developed, in order to guarantee to effectively improve Customer experience and gain customer loyalty. Reference should also be made to the opening of the TAP Premium Lounge in Lisbon, during the 1st semester of 2017, in a large area, aimed at offering passengers the most modern and comfortable rest areas in a reserved way, with various facilities available. Among these are shower cabinets, communication media (TV, free WIFI), flight information monitors, and a Business Centre, Bar and restaurant area which will provide an innovative catering service. The Premium Customer Centre will have a Space dedicated to passenger service.

Maintenance and Engineering

In the commercial context, and regarding TAP–Maintenance and Engineering Portugal, the perspectives for 2017 are of noticeable growth in relation to 2016, thanks to the contracts established for airframe, with both the introduction of sharklets on Qatar airplanes, and the executions of C inspections in KLM aircraft. The sales capacity of these services remains limited by the continuation of the reconfiguration programme of the interiors of the TAP fleet. A new tender of the French Air Force for its A310 fleet is expected this year; the result is difficult to predict in light of the two previous processes, which were discontinued. Regarding the Engine Maintenance business, the strategy developed in the meantime in search of opportunities and Customer loyalty allows the Company to be moderately optimistic, in particular with the 5-year contract signed with Tarom of Romania, comprising models CFM56-3, -5B and -7B.

In the operational perspective, the strong involvement of all Maintenance and Engineering continues in preparing the phase-out and phase-in, not only those which will take place in 2017, but also those which are already planned for 2018, naturally focusing on the preparation for the introduction of the A330-NEO and A321 NEO, so that it will happen without affecting TAP's Air Transport operation. Always with the aim of better serving our passengers, the second semester of 2017 will witness the start of a new partnership between Maintenance and Engineering and Panasonic, the company supplying entertainment and connectivity equipment for the Wide Body of the TAP fleet, so as to ensure a significant increase in reliability and operability. The components repair shop, due to investments already made, will have greater technological capacity, thus becoming better prepared to continue assisting the components which equip the new fleets. The operational areas of logistics and support will continue, both in the scope of Continued Improvement (whose number of events will double in comparison to 2016) and in the scope of specific projects with the support of external consultancy, with actions tending to increase process efficiency, reduce costs and optimise resource utilisation, while always guaranteeing high levels of safety and quality. In short, 2017 will be a year of continuity in the development and consolidation of a culture and practice intended to focus on results, commitments and innovation.

As regards Organization, and after all the work developed in 2016 which led to the FRA M certification, the ANAC certification of the new organizational structure is expected so as to highlight, within the current organization of Maintenance and Engineering, CAMO's responsibility centre, in charge of the activities connected to Continued Airworthiness. With respect to Innovation, Organization is to be developed for this reality which is much more than new tools or procedures but, rather, an organizational state of spirit and culture, which readily embraces change, the sharing of knowledge and mistakes made throughout each innovative course. In this sense, work will be done to obtain certification regarding the Portuguese law that regulates this matter.

In the Maintenance and Engineering business in Brazil, 2017 will continue to focus on the following objectives: i) improving production capacity and efficiency, which has been noticeable in Customer satisfaction reports and in obtaining new certifications; ii) improving commercial performance which, anchored in the previous point, has allowed a continuing revenue growth well above the growth of the MRO market in Latin America; iii) economic/financial sanitization. It is worth stressing the search for the optimization of synergies with Azul, the main Client of Maintenance and Engineering Brazil, aimed at increasing the volume and diversity of services provided and to establish an organizational restructuring programme to reduce costs.

It should be noted that TAP, SGPS, S.A. has a strategic vision for the future, one of its major objectives being to create a financially sustainable airline company, where one of its main strategic lines fleet-wise is to position itself among the best companies in the world, ensuring an ever more decisive role in the connections between Europe, Africa, Brazil and North America.

CONSOLIDATED FINANCIAL STATEMENTS

FINANCIAL YEAR OF 2016

TAP – TRANSPORTES AÉREOS PORTUGUESES, SGPS, S.A.

INDEX

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2016 AND 2015

Amounts stated in thousand euros	Notes	2016	2015
ASSETS			
Non-current assets			
Tangible fixed assets	5	718,963	641,001
Investment properties	6	2,248	2,216
Goodwill	7	172,060	149,791
Intangible assets	8	1,504	534
Other financial assets	13	40,560	1,100
Deferred tax assets	15	67,571	69,485
Other receivables	18	80,269	49,852
		1,083,175	**913,979**
Current assets			
Inventories	20	85,839	86,034
Trade receivables	21	187,999	138,130
Advances to suppliers	16	9,883	4,544
State and other public entities	17	22,985	17,427
Other receivables	18	62,548	59,652
Deferred expenses	19	17,296	13,272
Restricted cash	22	538	4,177
Cash and cash equivalents	22	150,468	136,814
		537,556	**460,050**
Non-current assets held for sale	23	36,355	-
		573,911	**460,050**
Total assets		**1,657,086**	**1,374,029**
EQUITY AND LIABILITIES			
Equity			
Share capital	24	15,000	15,000
Supplementary capital contributions	24	224,093	154,353
Legal reserves	24	3,000	3,000
Foreign currency translation reserves	24	(36,869)	(70,406)
Hedge reserves	24	(461)	(752)
Equity holdings adjustment		(2,260)	(2,260)
Retained earnings	24	(647,884)	(478,015)
Net income/(loss) for the year	24	(27,731)	(156,042)
Total equity of the Group		**(473,112)**	**(535,122)**
Non-controlling interests	25	3,475	4,807
Total equity		**(469,637)**	**(530,315)**
Non-current liabilities			
Provisions	26	26,441	26,126
Borrowings	27	666,841	743,370
Post-employment benefits obligations	28	67,688	54,268
Deferred tax liabilities	15	19,422	20,037
Other payables	31	105,479	84,019
		885,871	**927,820**
Current liabilities			
Suppliers	30	151,683	167,843
Advances from customers	29	1,403	1,259
State and other public entities	17	35,452	22,468
Borrowings	27	328,274	198,797
Other payables	31	314,870	250,960
Liabilities from unused flight documents	32	317,867	271,068
Deferred revenue	19	68,040	64,129
		1,217,589	**976,524**
Non-current liabilities held for sale	23	23,263	-
		1,240,852	**976,524**
Total liabilities		**2,126,723**	**1,904,344**
Total equity and liabilities		**1,657,086**	**1,374,029**

The accompanying notes form an integral part of the consolidated statement of financial position as at 31 December 2016.

CONSOLIDATED INCOME STATEMENT FOR 2016 AND 2015

Amounts stated in thousand euros	Notes	2016	2015 Restated
Sales and services rendered	35	2,289,638	2,408,722
Operating government grants	36	1,106	594
Gains and losses in associates	37	1,743	1,067
Variation in production	38	2,320	(8,589)
Internally generated assets	39	559	608
Cost of goods sold and materials consumed	40	(146,395)	(127,171)
External supplies and services	41	(1,511,112)	(1,664,382)
Employee costs	42	(585,831)	(556,957)
Impairment in inventory (losses/reversals)	43	(1,812)	206
Impairment in receivables (losses/reversals)	44	(2,129)	(5,655)
Provisions (increases/decreases)	45	1,442	170
Fair value increases/decreases	47	32	(174)
Other operational income	48	45,791	64,421
Other operational costs	49	(25,112)	(76,957)
Earnings before interests, taxes, depreciation and amortisation (before non-recurring items)		**70,240**	**35,903**
Non-recurring items	54	-	(91,394)
Earnings before interests, taxes, depreciation and amortisation		**70,240**	**(55,491)**
Depreciation and amortisation costs	50	(54,902)	(61,851)
Impairment of assets subject to depreciation/amortisation (losses/reversals)	46	(2,294)	-
Operating income/(loss) (earnings before interests and taxes)		**13,044**	**(117,342)**
Finance income	51	2,877	4,631
Finance costs	51	(44,190)	(67,904)
Net income/(loss) before income tax		**(28,269)**	**(180,615)**
Income tax for the year	52	(3,688)	20,176
Net income from continuing operations		**(31,957)**	**(160,439)**
Results from discontinued operations	23	8,944	8,662
Net income/(loss) for the year		**(23,013)**	**(151,777)**
Net income/(loss) attributable to owners of TAP SGPS		(27,731)	(156,042)
Net income/(loss) attributable to non-controlling interests	53	4,718	4,265
Basic and diluted earnings per share of continuing operations (Euros)	24	(21)	(107)
Basic and diluted results per share (euros)	24	(18)	(104)

The consolidated income statement for the year ended 31 December 2015 was restated considering the described in Note 23.

The accompanying notes form an integral part of the consolidated income statement as at 31 December 2016.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR 2016 AND 2015

Amounts stated in thousand euros	Notes	2016	2015
Net income/(loss) for the year		**(23,013)**	**(151,777)**
Items that may be reclassified to income statement:			
Gains and losses on translation of foreign operations	24	32,569	(50,903)
Gains and losses in derivate financial instruments - cash flow hedge	24	402	49,620
Deferred tax on derivative financial instruments - cash flow hedge	15	(111)	(13,645)
Items that will not be reclassified to income statement:			
Remeasurements of defined benefit plans	28	(16,109)	(2,761)
Deferred tax on remeasurements	15	2,172	812
Other comprehensive income/(loss) net of tax		**18,923**	**(16,877)**
Comprehensive income/(loss)		**(4,090)**	**(168,654)**
Attributable to:			
Owners of TAP SGPS		(7,730)	(169,680)
Non-controlling interests	53	3,640	1,026
Total comprehensive income/(loss) for the year		**(4,090)**	**(168,654)**
Comprehensive income/(loss) attributable to the owners of TAP SGPS arises from			
Continuing operations		(12,291)	(174,098)
Discontinued operations		4,561	4,418
		(7,730)	**(169,680)**

The accompanying notes form an integral part of the consolidated statement of comprehensive income as at 31 December 2016.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FROM 1 JANUARY 2015 TO 31 DECEMBER 2016

Amounts stated in thousand euros	Capital	Supplementary capital contributions (Note 24)	Legal reserves	Foreign currency translation reserves (Note 24)	Hedge reserves (Note 24)	Equity holdings adjustment	Retained earnings	Net income/(loss) for the year	Subtotal	Non-controlling interests (Notes 25 and 53)	TOTAL
Equity as at 1 January 2015	**15,000**	**-**	**3,000**	**(19,503)**	**(36,727)**	**(2,260)**	**(394,209)**	**(85,096)**	**(519,795)**	**7,935**	**(511,860)**
Transactions with owners in 2015	**-**	**154,353**	**-**	**-**	**-**	**-**	**(85,096)**	**85,096**	**154,353**	**(4,154)**	**150,199**
Application of net income/(loss) and distribution of profit and reserves	-	-	-	-	-	-	(85,096)	85,096	-	-	-
Supplementary capital contributions	-	154,353	-	-	-	-	-	-	154,353	-	154,353
Distribution of dividends to non-controlling interests	-	-	-	-	-	-	-	-	-	(4,154)	(4,154)
Comprehensive income/(loss) in 2015	**-**	**-**	**-**	**(50,903)**	**35,975**	**-**	**1,290**	**(156,042)**	**(169,680)**	**1,026**	**(168,654)**
Net income/(loss) for the year	-	-	-	-	-	-	-	(156,042)	(156,042)	4,265	(151,777)
Other comprehensive income/(loss)	-	-	-	(50,903)	35,975	-	1,290	-	(13,638)	(3,239)	(16,877)
Equity as at 31 December 2015	**15,000**	**154,353**	**3,000**	**(70,406)**	**(752)**	**(2,260)**	**(478,015)**	**(156,042)**	**(535,122)**	**4,807**	**(530,315)**
Transactions with owners in 2016	**-**	**69,740**	**-**	**-**	**-**	**-**	**(156,042)**	**156,042**	**69,740**	**(4,972)**	**64,768**
Application of net income/(loss) and distribution of profit and reserves	-	-	-	-	-	-	(156,042)	156,042	-	-	-
Supplementary capital contributions	-	69,740	-	-	-	-	-	-	69,740	-	69,740
Distribution of dividends to non-controlling interests	-	-	-	-	-	-	-	-	-	(4,972)	(4,972)
Comprehensive income/(loss) in 2016	**-**	**-**	**-**	**33,537**	**291**	**-**	**(13,827)**	**(27,731)**	**(7,730)**	**3,640**	**(4,090)**
Net income/(loss) for the year	-	-	-	-	-	-	-	(27,731)	(27,731)	4,718	(23,013)
Other comprehensive income/(loss)	-	-	-	33,537	291	-	(13,827)	-	20,001	(1,078)	18,923
Equity position as at 31 December 2016	**15,000**	**224,093**	**3,000**	**(36,869)**	**(461)**	**(2,260)**	**(647,884)**	**(27,731)**	**(473,112)**	**3,475**	**(469,637)**

The accompanying notes form an integral part of the consolidated statement of changes in equity as at 31 December 2016.

CONSOLIDATED STATEMENT OF CASH FLOWS FOR 2016 AND 2015

Amounts stated in thousand euros	Notes	2016	2015
Operating activities:			
Receipts from customers		2,363,288	2,709,810
Payments to suppliers		(2,079,817)	(2,089,045)
Payments to employees		(446,454)	(449,865)
Income tax payment/receipt		(5,032)	(16,459)
Other receipts/payments relating to operating activities		225,385	(165,128)
Cash flow from operating activities		**57,370**	**(10,687)**
Investment activities:			
Receipts from:			
Tangible fixed assets		64,666	74,571
Financial investments		116	1,043
Interests and similar income		2,665	4,526
Loans granted		-	2,900
Payments relating to:			
Tangible fixed assets		(143,409)	(47,463)
Intangible assets		(42)	-
Other financial assets		(39,276)	-
Cash flow from investment activities		**(115,280)**	**35,577**
Financing activities:			
Receipts from:			
Borrowings		227,650	635,344
Supplementary capital contributions	24	69,740	154,353
Payments relating to:			
Borrowings		(81,010)	(643,647)
Financial leasing contracts		(89,816)	(116,011)
Interests and similar costs		(42,909)	(46,620)
Dividends (non-controlling interests)		(5,622)	(3,504)
Cash flow from financing activities		**78,033**	**(20,085)**
Net increase (decrease) in cash and cash equivalents		20,123	4,805
Effects of exchange rate changes		(7,597)	(97,812)
Cash and cash equivalents at the beginning of the year		**140,991**	**233,998**
Non-current assets held for sale	23	**(2,791)**	**-**
Cash and cash equivalents at the end of the year	22	**150,726**	**140,991**

The accompanying notes form an integral part of the consolidated statement of cash flows as at 31 December 2016.

NOTES TO THE FINANCIAL STATEMENTS 31 DECEMBER 2016

1 - Economic activity of the Group

The Group, composed by TAP – Transportes Aéreos Portugueses, SGPS, S.A. ("TAP SGPS") and its subsidiaries ("TAP Group" or "Group") has its head office at Lisbon Airport and is dedicated to air transport operations involving passengers, cargo and mail, the implementation of maintenance and engineering works, providing handling services during air transport stopovers, exploration of duty free shops at airports and catering for aviation.

The Group's core business consists in the air transport of passengers, cargo and mail, operating in Portugal, mainland and its Autonomous Regions, Europe, Africa, North Atlantic, Mid-Atlantic and South Atlantic. The Group has 21 representative offices in foreign countries and 4 in Portugal.

Head Office	Lisbon Airport, Edifício 25
Share Capital	Euro 15,000,000
Taxpayer Number:	506 623 602

TAP – Transportes Aéreos Portugueses, SGPS, S.A. was incorporated on 25 June 2003 under Decree-Law number 87/2003, of 26 April, and its share capital was fully underwritten and paid-up in kind by Parpública - Participações Públicas, SGPS, S.A. ("Parpública"), through the entry of shares representing the entire share capital of the company Transportes Aéreos Portugueses, S.A. ("TAP S.A.").

As part of the TAP Group re-privatization process, on 24 June 2015 was signed the "Direct Sale Agreement" of TAP – Transportes Aéreos Portugueses, SGPS, S.A. ("TAP SGPS"), between Parpública (as seller), DGN Corporation ("DGN") and HPGB, SGPS, S.A. ("HPGB") (as proponents) and Atlantic Gateway, SGPS, S.A. ("Atlantic Gateway", currently adopting a limited corporation type) (as buyer), from which resulted the transmission of 915,000 nominal shares representative of 61% of the share capital of TAP SGPS to Atlantic Gateway on 12 November 2015, and Parpública remains with 39%.

Besides the "Direct Sale Agreement", it should be noted that, from among the various contractual instruments that have been formalised on 24 June 2015, the "Strategic Commitment Agreement", was formalised between the Portuguese State, Parpública, TAP SGPS, TAP S.A., DGN, HPGB and Atlantic Gateway, which establishes the terms and general conditions for the implementation of the "Strategic Plan", presented with the binding technical proposal, containing the measures that should contribute to the objectives of re-privatisation. Under this agreement, the parties assumed some strategic commitments, such as the promotion of the national hub e the maintenance of head office from TAP S.A. and Portugália – Companhia Portuguesa de Transportes Aéreos, S.A. ("Portugália") in Portugal.

With the transmission of 61% of the share capital of TAP SGPS to Atlantic Gateway on 12 November 2015, among other contractual instruments, it should be noted the “Agreement on Economic and Financial Stability of TAP” (“Acordo Relativo à Estabilidade Económica-Financeira”), between Parpública, Atlantic Gateway, TAP SGPS, TAP S.A. and Portugália, in which Atlantic Gateway, as buyer, and TAP S.A. and Portugália, as borrowers, assumed some obligations related to TAP Group financial debt and debt service.

As part of the process of notification to the Portuguese Civil Aviation Authority ("ANAC") of the transaction concluded on 12 November, 2015, which led to the acquisition by Atlantic Gateway of shares representing 61% of the share capital of TAP SGPS, should be noted that, by resolution of 19 February 2016, the Board of Directors of ANAC imposed a set of precautionary measures to the TAP Group. This proceeding with ANAC was, concluded favourably on 23 December 2016, at which date the Board of Directors of ANAC deliberated that TAP SA fulfilled the conditions set forth in Article 4 of Regulation (CE) nº 1008 / 2008 of the European Parliament and of the Council of 24 September 2008, on common rules for the operation of air services in the European Community.

Additionally, in December 2015 the Portuguese State informed Atlantic Gateway of its intention to review, by negotiation, the terms and conditions of its participation in TAP SGPS, namely through an increase in its participation in the equity of TAP SGPS, with Atlantic Gateway and its partners, HPGB and DGN, being willing to take part in the negotiation process proposed by the Portuguese State.

As this, on 6 February 2016, the Portuguese State and Atlantic Gateway formalised a "Memorandum of Understanding", which was amended on 26 April 2016, with the purpose of establishing the principles, rules and conditions to be followed by the parties during the revision of the participation of the Portuguese State, through Parpública, in TAP SGPS.

In accordance with the Memorandum of Understanding, Parpública, HPGB, DGN and Atlantic Gateway signed a purchase agreement on 19 May 2016, under which, once fulfilled certain precedent conditions, Atlantic Gateway undertook to sell shares representing the equity of TAP SGPS to Parpública, so that Parpública becomes the holder of 50% of TAP SGPS (the "Share Purchase Agreement"). Among the precedent conditions for the conclusion of this Agreement, we highlight the conclusion of the offer to sell shares representing up to 5% of TAP SGPS share capital to the Group’s employees, the necessary third party authorizations and the bank debt restructuration of TAP Group. The draft Shareholders' Agreement and Strategic Commitments of TAP SGPS to be signed between Parpública and Atlantic Gateway on the date of the conclusion of the Share Purchase Agreement ("Shareholders Agreement and strategic commitments of TAP SGPS") were attached to this Share Purchase Agreement.

The Resolution of the Council of Ministers nº 30/2016 of 19 May, which approved the minutes of the Share Purchase Agreement and the Shareholders Agreement and Strategic Commitments of TAP SGPS, also determined, among others, (i) the immediate cessation of the effects of the Strategic Commitment Agreement formalised on 24 June 2015, referred to above, on the date that the Shareholders Agreement and Strategic Commitments of TAP SGPS became effective, as well as (ii) the expiration of the unavailability scheme provided for in the specifications of the Reprivatization Process - with respect to the number of shares of TAP SGPS and TAP SA that are necessary to ensure the majority of the voting rights and effective control of mentioned companies - on the effective date of the transfer of the shares of TAP SGPS to Parbública.

Following the capitalization plan of the TAP Group defined under the scope of the Reprivatization Process, by resolution of TAP SGPS General Meeting on 8 March 2016, previously authorised by ANAC, was approved the issuance by TAP SGPS of a convertible bond into up to 130,800 special shares of the company in the amount of Euro 120 million and maturity in 10 years. The aforementioned issue is composed by two series: the first (series A), amounting Euro 90 million, subscribed by Azul Linhas Aéreas Brasileiras, SA ("Azul SA") on 16 March 2016, and the second (series B) in the amount of Euro 30 million subscribed by Parpública on 14 June 2016. The conversion of these bonds into shares of TAP SGPS and the collateralisation under this issue were subject to the express approval of ANAC, which occurred on 23 December 2016.

The consolidated financial statements reported herein, which include the assets, liabilities, costs and income of the TAP Group companies as listed in Note 2.3.1., were approved by the Board of Directors on 9 March 2017. However, these financial statements are still subject to approval by the General Meeting of Shareholders, under the terms of the commercial legislation in force.

The members of the Board of Directors that sign this report declare that, to the best of their knowledge, the information contained herein was prepared in conformity with the applicable accounting standards, providing a true and fair view of the assets and liabilities, the financial position and results of the companies included in the Group's consolidation scope.

2 - Summary of the principal accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are described below.

2.1 Basis of preparation

The Group’s consolidated financial statements have been prepared in accordance with International Financial Reporting Standards adopted by the European Union (IFRS – formerly referred to as the International Accounting Standards - IAS) issued by the International Accounting Standards Board (IASB) and the interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) or by the former Standing Interpretations Committee (SIC) in force on the date of preparation of the mentioned financial statements.

The accompanying consolidated financial statements were prepared on a going concern basis from the accounting books and records of the companies included in the consolidation (Note 2.3.1.) and under the historic cost convention, except for derivative financial instruments, investment properties and customer loyalty programs, which are recorded at fair value.

The preparation of the financial statements, accordingly IFRS, requires the use of important estimates and judgments in the application of the Group's accounting policies. Despite the estimates used are based on the best information available during the preparation of these financial statements and best knowledge of past and present events, we note that actual and future results may differ from these estimates. The principal statements which involve a greater degree of judgment or complexity and the most significant assumptions and estimates used in the preparation of the aforesaid financial statements are disclosed in Note 2.33.

The Group TAP and members of the Board of Directors that sign this report, declares that, to the best of their knowledge, the information contained herein was prepared in conformity with the applicable accounting standards, providing a true and fair view of the assets and liabilities, the financial position and results of the companies included in the Group's consolidation scope.

✈ **New standards, changes and interpretations of existing standards mandatory as at 31 December 2016:**

The application of the interpretations and amendments to the standards mentioned below, are mandatory by the IASB for the financial years beginning on or after 1 January 2016:

Description	Amendment	Effective date*
IAS 19 – Defined benefit plans	Accounting for contributions independent of years of service	1 February 2015
Annual improvements to IFRS's 2010 – 2012	Clarifications: IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16 and IAS 24	1 February 2015
IAS 16 and IAS 38 - Acceptable methods of depreciation / amortisation	Clarification that revenue based methods should not be used to measure the consumption of fixed and intangible assets' economic benefits	1 January 2016
IAS 16 and IAS 41 – Agriculture: bearer plants	Bearer plants are included within the scope of IAS 16, measured either at cost or revaluated amounts	1 January 2016
IFRS 11 – Joint arrangements	Accounting for acquisition of interest in a joint operation that is a business	1 January 2016
IAS 1 – Presentation of financial statements	Review of disclosures under the "Disclosure initiative" IASB project	1 January 2016
IAS 27 – Separate financial statements	Option to measure investments in subsidiaries, joint ventures and associates using equity method	1 January 2016
Amendments to IFRS 10, 12 and IAS 28: Investment entities - applying consolidation exception	Investment entities' exemption applies to an intermediate parent that is a subsidiary of an investment entity	1 January 2016
Annual improvements to IFRS's 2012 – 2014	Clarifications: IFRS 5, IFRS 7, IAS 19 and IAS 34	1 January 2016

** Financial years beggining on or after*

The introduction of the revision to this standard did not have any significant impact on the consolidated financial statements of the Group.

✈ New standards and interpretations not mandatory as at 31 December 2016:

There are new standards, interpretations and amendments of existing standards that, despite having already been published, are only mandatory for the periods starting on or after 1 January 2017, and which the Group decided not to early-adopt in the current period, as follows:

Standards and interpretations effective, on or after 1 January 2018:

Description	Amendment	Effective date*
IFRS 9 – Financial instruments	New standard for the accounting of financial instruments'	1 January 2018
IFRS 15 – Revenue from contracts with customers	Revenue recognition for the provision of goods or services, following a five step approach	1 January 2018

** Financial years beggining on or after*

Standards and interpretations effective, on or after 1 January 2017, not endorsed by EU:

Description	Amendment	Effective date*
IAS 7 – Cash flow statement	Reconciliation of changes in financing liabilities with Cash flows for financing activities	1 January 2017
IAS 12 – Income taxes	Accounting for deferred tax assets on assets measured at fair value, the impact of deductible temporary differences in future taxable income estimates and the impact of restrictions on the recoverability of deferred tax assets	1 January 2017
IAS 40 – Investment property	Clarification that evidence of the change in use is required, when assets are transferred to, or from investment properties category	1 January 2018
IFRS 2 – Share-based payments	Measurement of cash-settled share-based payments, accounting for modifications and classification as equity-settled share-based payments when employer withholds tax	1 January 2018
IFRS 4 – Insurance contracts (Applying IFRS 4 with IFRS 9)	Temporary exemption for insurance companies only, from applying IFRS 9 for annual periods beginning before 1 January 2021. Overlay approach for assets within IFRS 4 that qualify as FVTPL under IFRS 9 and at amortised cost under IAS 39, being the measurement difference reclassified to OCI.	1 January 2018
Amendments to IFRS 15 - Revenue from contracts with customers	Identification of performance obligations, timing of revenue recognition from licenses of IP, change to principle versus agent guidance, and new practical expedients on transition	1 January 2018
IFRS 16 – Leases	New definition of lease. New accounting of lease contracts to lessees. No major changes to lessors lease accounting.	1 January 2019
Annual improvements to IFRS's 2014 - 2016	Clarifications: IFRS 1, IFRS 12 and IAS 28	1 January 2017 and 1 January 2018
Interpretations		
IFRIC 22 – Foreign currency transactions and advance consideration	Foreign exchange rate to apply when consideration is paid or received in advance	1 January 2018

** Financial years beggining on or after*

Up to the date of issuing this report, the Group had not yet concluded the estimate of the effects of changes arising from the adoption of these standards, for which it decided not to early-adopt them. However, it does not expect them to have materially relevant impact on their equity position and results, with the exception of IFRS 16 - Leases.

2.2 Comparability of the financial statements

The figures presented in the consolidated financial statements for the year ended on 31 December 2016 are comparable in all significant aspects with the figures for the year ended on 31 December 2015.

2.3 Basis of Consolidation

2.3.1. Subsidiaries

Subsidiaries are all entities over which the Group considers control to exist.

The Group considers that there is control over an entity when the Group is exposed and/or has the right, as a result of its involvement, to the return of the entity's activities and has the capacity to affect that return through the existent control over that entity, namely when it holds direct or indirectly more than half of the voting rights. The existence and the effect of potential voting rights which are currently exercisable or convertible are taken into account when the Group assesses whether it has control over another entity.

Equity and net profit for the period corresponding to third party participation in subsidiaries are reflected separately in the consolidated statement of financial position and in the income statement, respectively in caption "Non-controlling interests" (Note 25).

The companies included in the consolidated financial statements are below detailed:

Name	Head office	Core business	Shareholders	% share capital held
TAP - Transportes Aéreos Portugueses, SGPS, S.A.	Lisboa	Management and administration of holdings	Parpública	39.00%
			Atlantic Gateway	61.00%
Transportes Aéreos Portugueses, S.A.	Lisboa	Aeronautical activities	TAP SGPS	100.00%
TAPGER - Sociedade de Gestão e Serviços, S.A. ("TAPGER")	Lisboa	Provision of management services	TAP SGPS	100.00%
Portugália - Companhia Portuguesa de Transportes Aéreos, S.A. ("Portugália")	Lisboa	Aeronautical activities	TAP SGPS	100.00%
Cateringpor - Catering de Portugal, S.A. ("Cateringpor")	Lisboa	*Catering*	TAPGER	51.00%
L.F.P. - Lojas Francas de Portugal, S.A. ("LFP")	Lisboa	Duty free shop operation	TAPGER	51.00%
Megasis - Soc. de Serviços de Engenharia e Informática, S.A. ("Megasis")	Lisboa	Engineering and provision of IT services	TAPGER	100.00%
U.C.S. - Cuidados Integrados de Saúde, S.A. ("UCS")	Lisboa	Provision of health care services	TAPGER	100.00%
Aeropar, Participações, S.A. ("Aeropar")	Brasil	Management and administration of holdings	TAP SGPS	99.83%
			Portugália	0.17%
TAP – Manutenção e Engenharia Brasil, S.A. (ex-VEM) ("TAP M&E Brasil")	Brasil	Maintenance and aeronautical engineering	TAP SGPS	51.00%
			Aeropar	47.64%

During the period ended at 31 December 2016 no changes occurred in the Group consolidation perimeter, however, the subsidiary L.F.P. - Lojas Francas de Portugal, S.A. was classified as non-current asset held for sale, due to the agreement to sell 51% of the share capital of the subsidiary's capital stock.

The purchase method is used in recording the acquisition of subsidiaries. The cost of an acquisition is measured by the fair value of the assets transferred, the equity instruments issued and liabilities incurred or assumed on acquisition date.

Transaction costs directly attributable to business combinations (consulting services, legal advice, administrative expenses, among others) are immediately recognised in the consolidated financial statements of the TAP Group as expenses of the year in which the acquisition took place, recognised in the consolidated statement of income.

The identifiable assets acquired and the liabilities and contingent liabilities assumed in a business combination are initially measured at fair value on the date of acquisition, irrespective of the existence of non-controlling interests. The excess of the acquisition cost relative to the fair value of the Group's share of the identifiable assets and liabilities acquired is recorded as Goodwill (Note 7).

Investments in subsidiaries where the TAP Group has control are fully consolidated from the date the Group assumes control over their financial and operating activities until the moment that control ceases to exist.

If the acquisition cost is less than the fair value of the net assets of the acquired subsidiary (negative goodwill), the difference is recognised directly in the income statement in the period when it takes place under "Other operational income"

Intercompany transactions, balances, unrealised gains on transactions and dividends distributed between group companies are eliminated. Unrealised losses are also eliminated, except where the transaction displays evidence of impairment of a transferred asset.

When, at the date of the acquisition of control, Group TAP already holds a previously acquired interest in the subsidiary, its fair value is considered in determining the goodwill or negative goodwill.

When Group TAP acquires control over a subsidiary with less than 100%, the purchase method considers non-controlling interests either at their fair value or in the proportion of the fair value of the assets and liabilities acquired. This decision is made for each individual transaction.

Subsequent transactions with non-controlling interest that do not result in loss of control are accounted for as equity transactions. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiaries is recorded in equity. Gain or losses on disposals to non-controlling interests are also recorded in equity.

Equity and net income, corresponding to the participation of third parties in subsidiary companies, are presented separately in the consolidated statement of financial position and in the consolidated income statement, respectively, under the heading of non-controlling interests. The losses and gains applicable to non-controlling interests are attributed to them.

Any contingent consideration to be transferred by the Group is recognised at fair value at the acquisition date. Any subsequent remeasures do not affect goodwill balances, except if made up to 12 months after the date of acquisition.

The subsidiaries' accounting policies have been adjusted whenever necessary to ensure consistency with the policies adopted by the Group.

2.3.2. Associates

Associates are all the entities in which the Group exercises significant influence but does not have control, which is generally the case with investments representing between 20% and 50% of the voting rights. Investments in associates are accounted for under the equity method.

In conformity with the equity method, financial investments are recorded at their acquisition cost, adjusted by the amount corresponding to the Group's share of changes in the associates' shareholders' equity (including net income/loss) with a corresponding gain or loss recognised for the period on earnings or on changes in capital, and by dividends received.

The difference between the acquisition cost and the fair value of the assets and liabilities attributable to the affiliated company on the acquisition date is, if positive, recognised as Goodwill and recorded as investments in affiliated companies. If negative, goodwill is recorded as income for the period under the caption "Gains and losses in associates".

In the event that impairment loss indicators arise on investments in associates, an evaluation of the potential impairment is made, and if deemed necessary, an impairment loss is recognised in the consolidated income statement. Impairment losses recognised in previous years may be reversed when it can be concluded that no impairment loss indicators exist.

Unrealised gains on transactions with associates are eliminated to the extent of the Group's investment in the associates. Unrealised losses are also eliminated, except where the transaction reveals evidence of impairments on the transferred assets.

The associates' accounting policies used in the preparation of the individual financial statements are adjusted, whenever necessary, to ensure consistency with the policies adopted by the Group.

The following entity qualifies as an associate:

Name	Head office	Core business	Shareholders	% share capital held
SPdH – Serviços Portugueses de Handling, S.A. ("SPdH")	Lisboa	*Handling*	TAP SGPS Portugália	43.90% 6.00%

The investments in associates are presented in detail in Notes 10 and 26.

2.4 Segment Reporting

As recommended by IFRS 8, the operating segments are presented on these financial statements in the same way as internally used for the Group's performance evaluation. Operating segment are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments. The Group does not disclose segmental assets and liabilities taking into consideration that this information is not presented to the chief operating decision-maker.

Four operational segments were identified: air transportation, maintenance and engineering, catering and others. It should be noted that the free shop activity is no longer considered as an operating segment, considering its classification as a discontinued operation (Note 23).

The accounting policies used in segment reporting are those consistently used in the Group. All inter-segmental sales and services rendered are made at market prices and eliminated on consolidation. Segmental information is disclosed in Note 55.

2.5 Foreign currency translation

2.5.1. Functional and presentation currency

The items included in the financial statements of each one of the Group's entities are measured using the currency of the economic environment in which the entity operates (functional currency). The consolidated financial statements are presented in Euro thousands, which is the Group's functional and presentation currency.

2.5.2. Balances and transactions expressed in foreign currencies

Transactions denominated in foreign currencies are translated into the functional currency using the exchange rates prevailing at the date of the transaction. Gains or losses resulting from the payment / receipt of transactions, as well as the translation of assets and liabilities denominated in foreign currencies using the applicable exchange rate at the reporting date, are recognised in the consolidated income statement under the caption financial results if related to loans, or in other operational income or costs if related to other balances/ transactions.

2.5.3. Group companies

The results and the financial position of the Group's entities that have a functional currency different from the Group's presentation currency are translated into the presentation currency as follows:

(i) The assets and liabilities presented are translated at the closing rate at the date of that statement of financial position. Exchange differences resulting from this conversion are recognised as a separate component in shareholders' equity under "Foreign currency translation reserves";

(ii) If materially relevant, the income and costs are converted at the exchange rate prevailing at the dates of the transactions. Otherwise, income and expenses are translated at the average monthly exchange rate of the reporting period.

Goodwill and fair value adjustments arising on the acquisition of foreign entities are treated as assets and liabilities of these entities and translated to Euro at the closing rate.

Exchange differences resulting from a monetary item, which forms part of the net investment in a foreign operation unit, are recognised in a separate component of equity and, when the net investment is sold or settled, are recognised in profit or loss as part of the gain or loss of the disposal.

The exchange rates used in the conversion of the financial statements expressed in a currency other than the Euro or to update balances expressed in a foreign currency were as follows:

Currency	2016	2015
BRL	3.4305	4.3117
USD	1.0541	1.0887
VEF	710.21	216.32
AOA	184.48	147.83

Regarding the subsidiaries located in Brazil, the monthly results were converted at the exchange rate of the last day of each month, as follows:

Month	2016	2015
January	4.4294	3.0114
February	4.3394	3.2579
March	4.1174	3.4958
April	3.9738	3.3232
May	3.9850	3.4522
June	3.5898	3.4699
July	3.6478	3.6974
August	3.6016	4.0671
September	3.6210	4.4808
October	3.4836	4.2724
November	3.6118	4.0709
December	3.4305	4.3117

2.6 Tangible fixed assets

Property, plant and equipment that were acquired prior to 1 January 2004 are recorded at their deemed cost, which is the book value under the accounting principles generally accepted in Portugal until 1 January 2004 (transition date to IFRS), including revaluations made in accordance with the prevailing legislation, deducted of depreciation and impairment losses.

Additionally, at transition date to IFRS, the subsidiary TAP S.A., under the exemptions of IFRS 1 - First-time Adoption of International Financial Reporting Standards – considered fair value as deemed cost for some tangible fixed assets categories, reported as at transition date (1 January 2004).

Thus, taking effect as at 1 January 2004, the assets related to the buildings category of TAP S.A. were revalued at their fair value on that date. The fair value of these items was determined through an evaluation study performed by an independent expert (Colliers P&I), which also determined the remaining useful life of these assets, on the transition date.

Property, plant and equipment acquired after the transition date are presented at cost, less accumulated depreciation and impairment losses. The acquisition cost includes all expenditure directly attributable to the acquisition of the assets.

Subsequent costs, including fleet renewals and structural maintenance, are included in the cost of acquisition of the asset whenever future economic benefits are likely to flow to the Group. The change in the accounting policy, related to the capitalization of structural maintenance, whose impact is not considered relevant in the financial statements, was recorded prospectively in the current year given the impracticability of its retrospective application due to its nature. Other costs with maintenance and repairs are recognised as losses in the period as are incurred.

Depreciation is calculated with regard to the acquisition cost, mainly using the straight line method from the date the assets are ready to enter into service, at the depreciation rates that best reflect their estimated useful lives, as follows:

	Years of useful life	Residual value
Buildings and other constructions	20-50	-
Basic equipment:		
Flight equipment:		
Airbus		
Aircraft	20	5%
Aircraft under financial leasing	20	5%
Spare engines and spare parts	20	5%
Spare engines under financial leasing	20	5%
Other flight equipment		
Aircraft	16	10%
Aircraft under financial leasing	16	10%
Spare engines and spare parts	16	10%
Spare engines under financial leasing	16	10%
Other basic equipment	7-20	0-10%
Transport equipment	4-10	-
Tools and utensils	8-20	0-10%
Administrative equipment	5-16	-
Other tangible fixed assets	10	-

The residual values of the assets and respective useful lives are reviewed and adjusted, when necessary, at the date of the statement of financial position (Note 5). If the book value of the asset is higher than the asset's realizable value, then it is written down to the estimated recoverable amount by recognizing an impairment loss (Note 2.10.).

Gains or losses arising from derecognition or disposal are calculated as the difference between the proceeds received on the disposal and the asset's book value, and are recognised in the income statement as other operating income or costs.

2.7 Investment Properties

Investment properties are buildings, land and other constructions held for capital valuation purposes, lease applications, or both. Investment properties were recognised at fair value at the date of transition to IFRS. After initial recognition investment properties are carried at fair value, for all assets classified as such.

The fair value of Investment properties are based on evaluations made by independent external evaluators, considering its usage conditions, or its best use, depending on whether the properties are leased or not.

2.8 Intangible assets

Intangible assets are booked at acquisition cost less accumulated impairment losses and are amortised using the straight line method over an estimated useful life. The amortisation period can be from 3 up to 10 years.

2.9 Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the identifiable assets, liabilities and contingent liabilities of the acquired subsidiary/associate at the date of acquisition by the Group.

Goodwill on acquisitions of subsidiaries and associates is not amortised and is tested, at least on an annual basis, for impairment. Impairment losses on goodwill cannot be reversed. Gains or losses on the disposal of an entity include the carrying amount of goodwill relating to that entity.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose, identified according to the operating segment.

2.10 Impairment of non-current assets

Non-current assets which do not have a defined useful life are not subject to depreciation, but are subject to annual impairment tests. Assets subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable.

If the recoverable amount is lower than net book value, an assessment is performed as to whether there is objective permanent evidence of impairment, and recognised the impairment loss in the income statement. If the loss is not considered permanent, the reasons that support the decision are disclosed.

An impairment loss is recognised as the amount of the excess of the asset's book value over its recoverable amount. The recoverable amount is the higher of the net sale price and its value in use.

For the purpose of conducting impairment tests, the assets are grouped at the lowest level for which cash flows can be identified separately (cash generating units which belong to the asset), when it is not possible to do so individually for each asset.

The reversal of impairment losses recognised in previous periods is recorded when it can be concluded that the recognised impairment losses no longer exist or have decreased (with the exception of impairment losses relating to Goodwill – see Note 2.9).

The reversal of impairment losses is recognised in the income statement as other operating income, except for the available-for-sale financial assets, unless the asset has been revalued, in which case the reversal will represent a portion or total of the revaluation reserve. However, an impairment loss is reversed only up to the limit of the amount that would be recognised (net of amortization or depreciation) if it had not been recognised in prior years.

2.11 Financial Instruments

The Group classifies its financial instruments in the following categories: loans and receivables, financial assets at fair value through profit and loss, held-to-maturity investments, and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its instruments at initial recognition and reassesses this classification on each reporting date.

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is no intention to settle on a net basis or realise the asset and settle the liability simultaneously. The legally enforceable right must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy of the company or the counterpart.

All acquisitions and disposals of these instruments are recognised on the date of the respective purchase and sale contracts, irrespective of the financial settlement date.

Financial instruments are initially recorded at the acquisition cost, when their fair value equals the price paid, including transaction expenses (except financial assets at fair value through profit or loss). The subsequent measurement depends on the category the instrument falls under, as follows:

- **Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments and which are not quoted in an active market. They are originated when the Group advances money, goods or services directly to a debtor without any intention of negotiating the debt.

These instruments are included in current assets, except when their maturity exceeds 12 months after the date of the statement of financial position, in which case they are classified as non-current assets.

Loans and other accounts receivables are initially measured at the fair value and subsequently at amortised cost and are included in consolidated financial statements in captions: “ Others receivables”, “Trade receivable” and “ Advances to suppliers”.

✈ **Financial assets at fair value through profit or loss**

A financial asset is classified under this category if acquired primarily for the purpose of selling in the short-term or if so designated by management. Assets in this category are classified as current if they are either held for trading or are expected to be realised within 12 months of the date of the statement of financial position. These investments are measured at fair value through the income statement.

✈ **Held-to-maturity investments**

Held-to-maturity investments are non-derivative financial assets, with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. Investments in this category are recorded at amortised cost using the effective interest rate method.

✈ **Available-for-sale financial assets**

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale at initial recognition or that do not meet the conditions to be classified in any of the remaining categories, as described above. Available-for-sale financial assets are classified as a non-current assets, except if management has the intention to sale the financial investment within 12 months after, the reporting date. These financial instruments are recognised at fair value, as quoted at the reporting date.

If there is no active market for a financial asset, the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same as the one in question, discounted cash-flows analysis and option pricing models refined to reflect the issuer's specific circumstances.

Potential fair value gains and losses arising from these instruments are recorded directly in the fair value reserve (shareholders' equity) until the financial investment is sold, received or disposed of in any way, at which time the accumulated gain or loss formerly reflected in fair value reserve is taken to the income statement.

If there is no market value or if it is not possible to determine one, these investments are recognised at their acquisition cost. At each reporting date the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired.

Impairment of financial assets

(i) Loans and receivables and held-to-maturity investments

The group assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired (difference between the recoverable amount and financial asset amount at the reporting date). The criteria that the Group uses to determine that there is objective evidence of an impairment loss include:

- Analysis of non-compliance;
- Failure to comply for more than 6 months;
- financial difficulties of the debtor;
- It becomes probable that the debtor will enter bankruptcy.

The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The asset's carrying amount of the asset is reduced and the amount of the loss is recognised in the consolidated income statement under the caption “Impairment in receivables”.

(ii) Available-for-sale financial assets

In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is also evidence that the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the consolidated income statement.

Impairment losses recognised in the consolidated income statement on equity instruments are not reversed through the consolidated income statement. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the consolidated income statement.

These categories of assets are derecognised when (i) the Group's contractual rights to receive their cash flows expire; (ii) the Group has transferred substantially all the risks and rewards associated with their detention; or (iii) not substantially all the risks and rewards associated with their holding, the Group has transferred control over the assets.

2.12 Derivative financial instruments

The Group uses derivative financial instruments to manage the financial risks to which it is exposed. Whenever expectations of changes in interest rates or jet fuel prices justify this, the Group seeks to hedge against adverse movements through derivative instruments, such as interest rate swaps (IRS), swaps and options.

The selection of derivative financial instruments is essentially driven by their economic properties. Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is initially recognised in other comprehensive income. Amounts accumulated in equity are reclassified to profit or loss in the periods when the hedged item affects profit or loss and recognised as operating income/(loss) for jetfuel instruments and as financial results for interest rate swaps, at their settlement date. The gain or loss relating to the effective portion of interest rate swaps is recognised in the income statement within ‘finance costs’. The gain or loss relating to the ineffective portion is recognised in the income statement.

Thus, expenses related to hedged debt are accrued for at the rate of its respective hedging operation. Gains or losses arising from early termination of this type of instrument, are recognised in the consolidated income statement when the hedged transaction also affects results.

Whenever possible, the fair value of derivatives is estimated on the basis of listed instruments. In the absence of market prices, the fair value of derivatives is estimated through the discounted cash-flow method and option valuation models, in accordance with prevailing market assumptions. The fair value of derivative financial instruments is included, essentially, in the headings of other receivables and other payables.

✈ Hedge accounting

The possibility of classifying a derivative financial instrument as a hedge instrument follows the provisions of IAS 39 – Financial instruments: recognition and measurement.

Derivative financial instruments used for hedging can be classified as hedge instruments for accounting purposes, provided that they cumulatively comply with the following conditions:

- ✈ On the starting date of the transaction, the hedge relationship is identified and formally documented, including the identification of the hedged item, the hedge instrument and the assessment of the effectiveness of the hedge;
- ✈ It is expected that the hedge relationship will be highly effective, on the starting date of the transaction and throughout the life of the operation;

- The effectiveness of the hedge can be measured reliably, on the starting date of the transaction and throughout the life of the operation;
- For cash flow hedge operations, it should be highly probable that they will occur.

2.13 Assets and liabilities fair value

The fair value measurements and related disclosures are based on a 'fair value hierarchy'. The hierarchy categorises the inputs used in valuation techniques into three levels.

Level 1 inputs are quoted prices in active markets for identical assets or liabilities that the Group can access at the reporting date.

Level 2 inputs are inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 inputs are unobservable inputs for the asset or liability. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. An entity develops unobservable inputs using the best information available in the circumstances, which might include the entity's own data.

2.14 Corporate Income Tax

Corporate income tax includes current and deferred tax. Current income tax is calculated based on net income, adjusted in conformity with tax legislation in place at the date of the statement of financial position.

Deferred taxes liabilities are recorded based on the temporary differences between the book values of the assets and liabilities and their respective tax base. Deferred tax assets are recognised whenever there is a reasonable likelihood that future taxable profits will be generated or there are deferred taxes liabilities against which they can be offset. Deferred tax assets are revised periodically and decreased whenever it is likely they will not be used.

The income tax rate expected to be in force in the period in which the temporary differences will reverse is used in calculating deferred tax.

Deferred taxes are recorded as a cost or income for the year, except where they result from amounts recorded directly under shareholders' equity, in which case deferred tax is also recorded under the same caption, i.e., the amounts to be included in the current tax and in the deferred tax, resulting from transactions and events recognised in reserves, are recorded directly in these same headings, not affecting the net profit for the period. Therefore, the impact of changes in the tax rate is also recognised in net income, except when it refers to items recognised directly in equity, in which case this impact is also recorded directly in equity.

2.15 Inventories

Inventories are valued in accordance with the following criteria:

- **Goods and raw materials**

Goods and raw, subsidiary and consumable materials are valued at the lower of their purchase cost or their net realizable value. The purchase cost includes ancillary costs and it is determined using the weighted average cost as the valuation method.

The inventories held essentially refer to parts used in aircraft maintenance activities.

Material recovered internally is valued at cost.

- **Intermediate products and work in progress**

Intermediate products and work in progress are valued at the lower of their production cost (which includes incorporated raw materials, labour and general manufacturing costs, based on a normal production capacity level) or their net realizable value.

The net realizable value corresponds to the estimated selling price after deducting estimated completion and selling costs. The difference between production cost and net realizable value, if lower, are recorded as an operational cost in caption "Impairment in inventories".

2.16 Trade and other receivables

Debtors' balances and other current assets are initially recorded at fair value and are subsequently recognised at their amortised cost, net of impairment losses, in order to present those balances at their net realisable amount (Notes 16, 18 e 21).

Impairment losses are recognised when there is objective evidence that the Group will not receive the full amount outstanding in accordance with the original conditions of the accounts receivable.

2.17 Cash and cash equivalents

Cash and cash equivalents includes cash, bank accounts and other short-term investments with an initial maturity of up to 3 months which can be mobilised immediately without any significant risk of fluctuations in value. For the purposes of the cash flow statement, this heading also includes bank overdrafts, which are presented in the statement of financial position, in current liabilities, under the heading " Borrowings".

The Group records the cash and cash equivalents, whose repatriation is restricted, in the heading "Restricted cash" under current assets.

2.18 Share capital and own shares

Ordinary shares are classified in shareholders' equity (Note 24).

Costs directly attributable to the issue of new shares or other equity instruments are reported as a deduction, net of taxes, from the proceeds of the issue.

Costs directly attributable to the issue of new shares or options for the acquisition of a new business are included in the acquisition cost as part of the purchase consideration.

Own shares are recorded at their acquisition value, as a reduction of equity, under the heading "Own shares", with any gains or losses inherent to their disposal being recorded under other reserves. Pursuant to the applicable commercial legislation, while own shares are held by the company, a reserve of an amount equal to their acquisition cost is unavailable.

2.19 Borrowings

Borrowings are initially recognised at fair value, net of the transaction costs incurred and are subsequently stated at their amortised cost. Any difference between the amounts received (net of transaction costs) and the amount to be repaid is recognised in the income statement over the term of the debt, using the effective interest rate method.

Borrowings are classified as a current liability, except when the Group has an unconditional right to defer the settlement of the liability for at least 12 months after the date of the statement of financial position (Note 27).

2.20 Borrowing Costs

Borrowing costs relating to loans are usually recognised as financial costs, in accordance with the accrual principle.

Financial costs on loans directly related to acquisition of the fixed assets, construction (if the construction period or development exceeds one year) or production, are capitalised as part of the asset's cost.

Capitalisation of these charges begins once preparations are started for the construction or development of the asset and is suspended after its utilization begins or when the respective project is suspended.

2.21 Provisions

Provisions are recognised whenever the Group has a present legal or constructive obligation, as a result of past events, in which it is probable that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated.

Provisions for current lawsuits are recorded in accordance with the risk assessments carried out by the Group and its legal advisors, based on historical success rates by nature of legal action and probability of unfavourable outcomes for the Group.

Provisions for future operating losses are not recognised. Provisions are reviewed on the date of the statement of financial position and are adjusted to reflect the best estimate at that date (Note 26).

2.22 Post-employment benefits

Some of the Group's companies have undertaken to make payments to their employees for complementary retirement pension, early retirement, health care and seniority bonuses.

As referred in Note 28, the Group set up autonomous Pension Funds as a means of funding most of the commitments for such payments. The total liability of Post-employment benefits referred above is estimated, periodically, by a specialised and independent entity in accordance with the projected unit credit method.

Remeasurements resulting from differences between the assumptions used for purposes of calculating the liabilities and what effectively occurred (as well as from changes made thereto and from the difference between the expected amount of the return on the funds' assets and the actual return) are recognised when incurred directly in the consolidated statement of comprehensive income.

The liability thus determined is stated in the statement of financial position, less the market value of the funds set up, as a liability, under the caption "Post-employment benefits obligations".

Plans that have surplus funding are recorded as assets, when there is explicit authorization for their offsetting with future employer contributions, or if the reimbursement of this financial surplus is explicitly authorised or permitted.

Gains and losses generated on a curtailment or settlement of a defined benefit pension plan are recognised in the income statement when the curtailment or settlement occurs. A curtailment occurs when there is a material reduction in the number of employees or the plan is altered in such a way that the benefits awarded are reduced with a material impact.

Past-service costs that results from the implementation of a new plan or increases in the benefits attributed are recognised immediately in income statement.

For defined contribution plans, the Group pays contributions to pension insurance plans on a mandatory, contractual or voluntary basis. The group has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they are due.

2.23 Suppliers and other payables

Current suppliers and other payables are, initially, recorded at their fair value and, subsequently, at amortised cost (Notes 29, 30 and 31).

2.24 Government grants

Government grants are recognised when there is a reasonable assurance that the grant will be received and the group will comply with all required conditions.

Government grants related to operating costs are deferred and recognised in the income statement over the period that matches the costs with the compensating grants.

Government grants received to compensate capital expenditure are reported under "Other payables" and are recognised in the income statement during the useful life of the asset being financed, by deducting the value of its depreciation/amortisation.

2.25 Leases

Fixed assets acquired under leasing contracts, as well as the corresponding liabilities, are recorded using the finance method.

According to this method, the asset's cost is recorded in Tangible fixed assets and the corresponding liability is recorded under liabilities as Borrowings, while the interest included in the instalments and the asset's depreciation, calculated as described in Note 2.6, are recorded as costs in the consolidated income statement of the period to which they relate.

Leases under which a significant part of the risks and benefits of the property is assumed by the lessor, with the Group being the lessee, are classified as operating leases. Payments made under operating leases, net of any grant received by the lessee, are recorded in the income statement during the period of the lease.

2.26 Dividends distribution

The distribution of dividends to shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the shareholders and up until the time of their payment.

2.27 Revenue and accrual basis

Income from sales is recognised in the consolidated income statement when the risks and benefits inherent in the ownership of the respective assets are transferred to the purchaser and the income can be reasonably quantified.

Revenue from the sale of passenger and cargo transport is recorded as a liability when the sale is made, under the heading "Liabilities from unused flight documents". When the ticket is used or cancelled, its value is transferred from this heading to the income statement for the year or to an account payable, depending on whether the transport has been: i) carried out by the Group or the ticket has been cancelled and is not subject to reimbursement ii) made by another airline carrier or the ticket has been cancelled but is subject to reimbursement, respectively, by a value which is usually different from that recorded at time of its sale. Periodically, the balance of "Liabilities from unused flight documents" is analysed to adjust the balance of tickets sold to check for those that have already been used or that are no longer valid and thus, not suitable for flight or reimbursement.

Commissions attributed by the Group on ticket sales are deferred and recorded as costs for the year, according to the distribution of the periods between years of the respective transport revenue.

For the "TAP Victoria" frequent flyer program, the Group follows the procedure, under defined conditions and based on flights carried out, of granting free air miles to customers who join the loyalty scheme, which may subsequently be used for flights with favourable conditions, such as reduced fares. Based on the number of miles attributed and not used or expired at the end of each year, adjusted to the estimate of the miles to expire without use and on the unit value attributed, at fair value, the Group defers the revenue corresponding to the estimate of the value perceived by the customer in the attribution of miles.

For purposes of the recognition of revenue of work in progress from maintenance contracts, Group recognises only to the extent of contract costs incurred that it is probable will be recoverable. It should be noted that, generically, maintenance contracts periods are less than three months.

Contract costs are recognised as a cost in the year in which they occur. When it is likely that the total costs of the contract will exceed the total revenue, the expected loss is recognised as an expense.

The preliminary invoicing of maintenance work in progress for third parties as at 31 December 2016 is recorded under the caption “Deferred revenue”.

Revenue is shown net of value-added tax, returns, rebates and discounts and comprises the fair value of the consideration received or receivable for the sale of goods.

Group companies record their costs and income according to the accrual basis of accounting, so that costs and income are recognised as they are generated, irrespective of the time at which they are paid or received.

The differences between the amounts received and paid and the respective costs and income are recognised as deferred expenses and revenues, other receivables and payables (Notes 19, 18 and 31, respectively).

2.28 Non-recurring items

Accordingly to paragraphs 85 and 86 of IAS 1, the non-recurring items recognised in the consolidated income statement reflect unusual expenses that should be presented in a separate line item, considering its magnitude and relevance to an understanding of the Group's operations and results.

2.29 Contingent assets and liabilities

Contingent liabilities in which the probability of an outflow of funds affecting future economic benefits is not likely, are not recognised in the consolidated financial statements, and are disclosed in the notes, unless the probability of the outflow of funds affecting future economic benefits is remote, in which case they are not disclosed.

Provisions are recognised for liabilities which meet the conditions described in note 2.21.

Contingent assets are not recognised in the consolidated financial statements but are disclosed in the notes when it is probable that a future economic benefit will arise from them.

2.30 Non-current assets and liabilities held for sale and discontinued operations

Non-current assets are classified as non-current assets held for sale when is intended to be recovered mainly through a sale transaction rather than continued use and there is a decision of the Board of Directors with the consequent definition of the price and buyer demand, which allows to classify the sale transaction, as a highly probable realization, in the period up to 12 months.

These assets are measured at the lower of book value and fair value less costs to sell, at the date of classification as held for sale. Assets with defined useful lives are no longer depreciated/amortised from the date of classification as held for sale, up to the date of sale.

A discontinued operation is a component of the TAP Group that has either been disposed of or is classified as held for sale and:

- Represents an important business line or separate geographic area of operations;
- It is a part of a single coordinated plan to dispose of an important separate line of business or geographical area of operations; or
- It is a subsidiary acquired exclusively with the purpose of resale.

2.31 Consolidated statement of cash flow

Consolidated statement of cash flow is prepared in accordance IAS 7, through direct method. Cash and cash equivalents includes cash, bank accounts and other short-term investments with an initial maturity of up to 3 months which can be mobilised immediately without any significant risk of fluctuations in value.

For the purpose of the consolidated cash flow statement, this heading also includes bank overdrafts, which are presented in the consolidated statement of financial position, under the heading "Borrowings ", as well as "Restricted cash".

The cash flows are presented in the consolidated cash flow statement, depending on their nature, into (1) operating activities, (2) investment activities and (3) financing activities.

Operating activities essentially include revenue from customers, and payments to suppliers and employees. These activities also include payments of net indirect taxes, income tax and payments related to post-employment benefit obligations.

The cash flow from investing activities includes, namely, acquisitions and disposals of financial investments, dividends received from associate companies, and revenue and payments arising from the purchase and sale of tangible and intangible assets.

The cash flow from financing activities includes, namely, the payments and receipts related to loans obtained, payments with interests and related expenses, own shares acquisition and payment of dividends.

2.32 Subsequent events

Events after the date of the statement of financial position which provide additional information about the conditions prevailing at the date of the statement of financial position are reflected in the consolidated financial statements.

Subsequent events which provide information about conditions which occur after the date of the statement of financial position are disclosed in the notes to the consolidated financial statements, if material.

2.33 Important accounting estimates and judgments

The preparation of consolidated financial statements requires that the Group's management makes judgments and estimates that affect the amount of revenue, costs, assets, liabilities and disclosures at the date of the statement of financial position.

These estimates are influenced by the Group's management's judgments, based on: (i) the best information and knowledge of present events and in certain cases on the reports of independent experts; and (ii) the actions which the Group considers it may have to take in the future. However, on the future date on which the operations will be realised, the outcome could be quite different from those estimates. Pursuant to IAS 8, any changes to these estimates, which occur after the date of the consolidated financial statements, are adjusted prospectively through income statement.

The estimates and assumptions which present a significant risk of generating a material adjustment to the book value of assets and liabilities in the following financial period are presented below:

- **Impairment of goodwill**

The Group tests the goodwill carried in its statement of financial position for impairment losses annually, in accordance with the accounting policy described in Note 2.9. The recoverable amounts of the cash generating units are ascertained based on the calculation of their value-in-use. These calculations require the use of estimates.

The estimated value in use involves a high degree of judgement by the Board of Directors, regarding the determination of estimated cash flows, applicable discount rates and residual values.

- **Deferred tax**

The Group recognises and settles income tax based on the earnings of its operations, calculated in accordance with the local corporate legislation, considering the rules of the tax legislation, which are different from the values calculated in accordance with the IFRS. Pursuant to IAS 12, the Group recognises deferred tax assets and liabilities based on the existing difference between the book value and tax base of its assets and liabilities. The Group periodically analyses the recoverability of the deferred tax assets based on historical information on taxable profit, the projection of future taxable profit and the estimated time of reversal of temporary differences.

- **Post-employment benefits**

Liabilities relating to defined-benefit plans are calculated based on actuarial assumptions. Changes to those assumptions can have a material impact on the aforesaid liabilities. The key assumptions for pension obligations are detailed in Note 28. The Group's policy is to periodically review the main demographic assumptions, when their impact on the consolidated financial statements is considered relevant.

- **Recognition of provisions and impairments**

The Group is involved in several lawsuits, for which, based on the opinion of its lawyers, a judgment is made in order to decide if it should be recorded a provision for those contingencies.

Impairment losses in trade receivables are booked essentially based on the analysis of the ageing of accounts receivable, the customers' risk profile and their financial situation.

Impairment losses in inventories are calculated based on criteria's that consider the nature, purpose of use, ageing and moving average stock levels.

- **Customer loyalty program**

The deferral of revenue related with the customer loyalty program "TAP Victoria", is based on the unit value of the mile perceived by the customer. Changes in the assumptions used by the Group in the calculation of this estimate may have a significant impact.

- **Liabilities from unused flight documents**

The Group carries out a periodic analysis of the balance of the caption "Liabilities from unused flight documents" in order to correct the values of tickets sold whose vouchers are no longer valid. The estimation of the amounts of these coupons, which cannot be exchanged or reimbursed, requires judgment by the Board of Directors, and therefore changes in the assumptions used by the Group in calculating this estimate may have a significant impact on the consolidated financial statements.

✈ **Useful life and residual value of tangible fixed assets**

The determination of the useful life of tangible fixed assets and their residual value, as well as the method of depreciation/amortisation, is essential to estimate the amount of depreciation/amortisation to be recorded in the consolidated income statement for each financial year.

These parameters are defined in accordance with the best judgement of the Board of Directors for the referred assets in question, also considering the practices adopted by peers.
See additionally Note 5.

✈ **Fair value of derivatives and other financial instruments**

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. The Group uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period.

✈ **Venezuela rate exchange**

Following the strong deterioration of the Venezuelan economy, the successive devaluations of the local currency and the current limitation to the repatriation of capital controlled by local government entities, the Group has been periodically monitoring the timing of the repatriation of the amounts indicated and applicable rate exchange in order to obtain the best possible estimate as at 31 December 2016.

The future currency fluctuations and future capital repatriation policies are not under Group’s control, thus a different completion may result in significant impacts in the future, which could affect the operating results and the Group’s financial position. See additionally Note 22.

3 – Financial risk management policies

Risk management is conducted at the strategic level by the Group and subject to ongoing monitoring by the management board. The defined guidelines and decisions adopted regarding risk management are key elements for the positioning of the Group in the face of external threats of the markets and the economic and financial environment. Given the multiplicity of scenarios and possible developments, the Group's risk management strategy incorporates elements of flexibility and discretion to allow adjustment in a timely basis to changes in the general context.

The Group's activities are exposed to a variety of financial risk factors, including the effects of market price changes, namely fuel price risk, currency risk, interest rate risk, as well as credit risk and liquidity risk.

The Group's risk management is driven and monitored by the Board of Directors and is executed by competent management areas of the Group, in particular, with regard to financial instruments risk management, including derivative fuel operations, interest and exchange rate, by the corporate finance department of TAP SA, following the guidelines and policies defined and disclosed as well as specific instructions issued.

✈ Market risk

Competition in commercial aviation has intensified in recent years as a result of the increasing liberalization of regulation in many countries and markets and as a consequence of the increase in the number of players in the sector.

In Europe the level of competition is very high in most markets and low-cost operators have successively achieved a larger market share. In Portugal the level of penetration of low cost airlines is, for example, about one-third at Lisbon airport, and in Oporto has the majority market share.

Also in the long-haul there is an increasing competition between operators given the various alternative routes available to the same destination. Madrid, for example, can easily compete with Lisbon in attracting traffic originating in Brazil and bound for multiple European cities. This dispute has actually occurred on some Brazilian routes between TAP and TAM. Similarly, in the North Atlantic, TAP tries to divert traffic from other routes and to attract US passengers, or that go to the US, to pass through the Lisbon hub.

Competition on a day-to-day basis is based on the price factor, including the stratification of supply in several fare classes on the same flight and on the same aircraft. However, in the medium and long-haul, competition and market risks are faced by airlines through the construction of business models, route networks, and products that satisfy the customer in the various aspects valued.

This differentiated product incorporates elements such as reliability, regularity, timeliness, diversity of schedules, flight frequency, equipment comfort, in short, product quality, quality in flight experience. Many of these aspects are inevitably linked to the characteristics of the aircraft, which have to be comfortable, modern, technologically advanced and also economically efficient, with low consumption, low noise, low emissions and flexible in terms of flight autonomy. A modern and advanced fleet is a fundamental asset to compete.

Immediately after the reprivatisation of the Group in November 2015, TAP began an ambitious strategic plan for the global fleet renewal, to be implemented in several stages. A cycle of massive investment and deep renewal of the airline was beginning. This cycle, which will last for several years, includes the renewal of most of the current fleet of 20 long-haul aircraft and 43 medium-haul aircraft, replacing for 53 new aircraft ordered to Airbus in 2015 to be delivered from 2018 onwards. This order involved, early in 2016, a first phase of investment by TAP in pre delivery payments paid to the manufacturer and will require a high and continuous financial effort during the coming years.

Given that the planned deliveries of the new aircraft will take place gradually from 2018 onwards, TAP has prepared an interim renewal program for the existing fleet, including the improvement of the cabin interior of the aircraft, in order to provide passengers with greater comfort and greater flexibility for the company to manage the space to be sold. This cabin modification program was started in 2016 and will continue in 2017, covering a substantial part of the aircraft of both mid and long-haul fleets. The retrofit interventions are mostly carried out both in Maintenance and Engineering in Portugal and Brazil. In addition to the cabin upgrade of aircraft, other investments were initiated or carried out in 2016 such as the installation on the wings of some aircrafts, devices designed to reduce fuel consumption - sharklets. It is estimated that these devices reduce fuel consumption by 4% and that the required investment recovery time is less than 3 years.

TAP Maintenance and Engineering is the 1st MRO (Maintenance, Repair and Overhaul) in Europe, and 2nd in the world, to carry out the installation of sharklets. Finally, in addition to the modernization of the existing fleet and in order to a short-term reinforcement of the available capacity, namely to operate the new routes launched in 2016, two leased A330 aircraft entered into the operation.

The medium and long-haul fleets had, in 2016, an average age above 15 years. However, the TAP Group's regional fleet had a much higher average age at the beginning of the year. The fleet of Portugália in early 2016 comprised 6 Fokker 100 (97 seats) and 8 Embraer 145 (49 seats), with average ages of 25 and 20 years old, respectively. The TAP Group successfully completed in 2016 the full restructuring of the regional fleet operated by Portugália through the leasing of nine Embraer 190 aircrafts.

On the other hand, TAP S.A. also contracted for the regional service with White Airways, S.A. ("White"), the lease of eight ATR72 aircraft in order to complement the capacity required for the regional network. During the year, were received and integrated into the operation 9 Embraer 190 aircrafts (106 seats) operated by Portugália, and 8 ATR72 aircrafts (70 seats) operated by White and serving TAP SA under wet lease (lease with crew).

The average age of the ATR72 aircrafts was about 1 year at the time of entry into service and the average age of the Embraer 190 aircraft was approximately 5 years. These aircrafts, practically new, are more efficient, have lower operation and maintenance costs, are technologically advanced, have more seats and more cargo capacity. The year of 2016 was a period of transition and adaptation in which the Embraer 190 operated during approximately half of the year while the ATR72 operated a little more than half of the year 2016. In the autumn was concluded the operation of the old aircrafts which will be discontinued.

The network underwent a series of adaptations and adjustments during 2016, and some European routes were cancelled and closed also, for example, in the long-haul, the route of Colombia and the route of Manaus. On the other hand, the routes of Boston and New York-JFK, in the USA, were launched, as well as the air-bridge between Lisbon and Oporto with a significant number of daily frequencies.

The number of passenger kilometres offered (PKO) in Portugal mainland increased by 50% in 2016. In Europe the PKO variation was close to 6% and in the US the PKO number increased by more than 60%. On the other hand, TAP S.A. had to adjust its operation in Brazil (with a 35% weight in the total of the operation) and also in Angola. PKOs decreased 10% on Brazilian routes and close to 20% on the Luanda route. Overall network PKO decreased 3% as a result of the combined effect of all positive and negative variations in the various geographic areas. The load factor remained unchanged from 2015 to 2016, with the number of passenger kilometres used (PKU) also falling 3% in line with the PKO decline. The decline of the 2016 PKU compares with the 1.6% reduction recorded in 2015 and a 7% increase in 2014, the year of expansion of the operation. In terms of average revenue per PKU, or yield, there was a decrease in 2016 of 2%, against reductions of 3.5% in 2015 and 7% in 2014.

The reduction in ticket revenues in 2016 was 5% compared to 2015, resulting from a 2% yield decline and a 3% reduction in activity. In particular, the decline in yield reflects, in addition to the geographical mix of the TAP S.A. operation, also the overall context of lowering fares that most companies practiced in search of market share and taking advantage of lower fuel costs. The total revenue from tickets was reduced by more than Euro 100 million to approximately Euro 2 billion.

In Brazil, ticket sales fell by around 20%, as a result of the deep economic crisis and the strong impact of private consumption in the year. However, the reduction in income on an intra-annual basis was more subdued in the second half of the year, by 10% year-on-year, compared to more than 30% in the first half of the year, reflecting a gradual stabilization of the situation. Given the weight and the total value of the revenues of Brazil, above 400 million Euro in 2015, about one fifth of the total sales, the fall in this market was the fundamental conditioning factor of the revenue in 2016.

The Portuguese market, which accounted for around Euro 450 million in revenues, recorded a 4% drop in the value of sales, with a decrease in the average fare practiced partially offset by the increase in tickets sold.

The United States saw its sales volume increase by 35% and had a share of TAP S.A. sales of 8% of the total sales, higher than all African markets, with 7%. This was pushed by the consolidation of the Miami line as well as the beginning, in the middle of the year, of the two new routes, Boston and JFK.

In Africa, Angola recorded a 20% drop in revenues in relation to 2015, in line with the reduction in supply on the Luanda route in the same order of magnitude. It was possible, through this capacity adjustment, to maintain the level of the average fare in either in dollar or euro.

In 2016, cargo transport activity fell by almost 15%. The reduction in revenues resulted from a decrease in the transported tonnage of almost 10% and a reduction of cargo yield of 5%. Cargo sales fell more than 20% in Portugal but this reduction was closely related to the behaviour of Brazil as the main destination market. Also, as a market that exports cargo, Brazil has dropped by around 15% in 2016. Other important markets, such as

Germany and Italy, have decreased their cargo revenues, since the exports in question are normally destined for Brazil and Angola. From the group of markets with greater weight, only the United States increased cargo sales, by 8%, as a result of the significant increase in the number of flights to and from the US.

The maintenance activity for third parties registered a significant decrease in 2016, in Maintenance and Engineering in Portugal. The main reason for the decrease was a significant reduction in aircraft work in terms of fuselage to third parties. On the contrary, there was an increase in reactors, although insufficient to compensate for the decrease in aircrafts and components work. The decrease in airframe work for third parties was precisely related to the increase of the work for the TAP fleet, due in particular to the ongoing cabin modification programme.

In the maintenance and engineering unit in Brazil, on the other hand, there was an increase of approximately 30% in revenues from third parties, corresponding to a higher volume of work done.

✈ **Fuel price risk**

In commercial aviation markets, airlines are particularly subject to the impact of changes in international energy markets that determine their fuel costs. This cost is, in the TAP Group, the component with the most weight in the operating expenses structure. On the other hand, it is a cost component with extreme volatility and that is decisive for the operating result, as well as for the definition of the fare conditions and market policies, in each year.

In 2016 the crude oil price fell, in average, comparing with the previous year, 17%. On the other hand, the prices of the Platts index of jet fuel registered in 2016 a reduction, in average, near 20%. The decline in the price recorded in 2016 has accentuated the trend already seen since mid-2014, when the brent stood at 110 dollars per barrel. From then on it would fall to close to 60 dollars by the end of 2014 and later, about 50% during the year 2015, reaching minimum values below 30 dollars by the end of 2015.

During 2016, however, the price of crude oil registered a gradual recovery, ending the year above 50 dollars per barrel. The average price of 2016, about 43 dollars per barrel, was still 10 dollars below the previous year's average. The price of jet fuel, as well as most of refined products, also fell in line with crude oil, with the average jet fuel price, namely the CIF NWE reference, lowered by 100 dollars from 2015 to 2016, from 525 dollars for 425 dollars per ton, ending the year 2016 marginally above 500 dollars per ton.

During 2015 hedge operations were contracted covering approximately 50% of the projected exposure. Given the subsequent decline in energy markets, the hedging process was suspended in the second half of 2015, so that by the end of the year all hedging operations had been extinguished and there was no need to record any unfavourable hedge reserves in 2015 and 2016.

The maintenance of crude oil prices and the low jet fuel price during 2016 had a significant impact on operating results, with total fuel costs reducing by one third in 2016 compared to 2015, considering the impact of risk coverage of the price of jet fuel materialised during this period.

Fuel expenses decreased to Euro 434 million in 2016 from Euro 660 million recorded in 2015. The average price of jet fuel in dollars paid by TAP SA was 20% lower than in the previous year, when in 2015 had already been less than 2014 by 40%. Given that there were several hedging operations in force in 2015, negotiated prior to the rapid decline in prices at the end of 2014, the cumulative effect of the price depression of 2015 and 2016 only had full effects in the year 2016, a year in which already there was no unfavourable impact on the TAP Group's accounts of fuel price hedging operations. The variation of the dollar against the euro did not have a significant impact in 2016, compared to 2015, as the average exchange rate variation for the year as a whole was less than 1%. The volumes consumed, close to 1 million tons of jet fuel, decreased in the year by approximately 3% in line with the reduction in flight hours compared to the previous year.

The TAP Group did not have fuel price hedging operations in place for 2017 at the end of the year 2016, so that it could benefit fully from any maintenance of the low price environment.

As at 31 December 2016 a variation (positive or negative) of 10% in the jet fuel price, would result in an impact on the income statement of some Euro 43 million.

✈ **Currency risk**

The TAP Group's overall foreign exchange exposure in all the markets in which it operates is significant due to its operation on more than 100 routes in three continents, and also the significance of the routes between Europe and the American continent in air transport activity, in addition to its involvement in Brazil in terms of industrial investment in aircraft maintenance and engineering activity. To the risks inherent to exchange rate fluctuations and exchange rate policy decisions of the monetary authorities of countries with controlled exchange systems, joins the sovereign risks such as the one that occurred in Venezuela due to its economic and financial collapse.

At the level of revenues, Brazil has been losing weight in the total sales of TAP SA with successive breaks of revenue in that market since the peak of 2013, having reduced its share to 17% in 2016. This was the year in which the decline in revenue was more pronounced, with a 20% reduction. The decline in sales in Brazil was clearly influenced by the deep economic recession experienced in the last three years in the country and the strong contraction in consumption. In the year 2016 there were no significant fare changes but the market reacted again to the reduction of the purchasing capability through the use of tickets with lower prices, lowering the fare level.

On the other hand, since fares were defined in US dollars, and the Real appreciated moderately in 2016 in average against the dollar, the exchange rate contributed, although marginally, to an automatic, downward adjustment of the prices in Brazilian Real, favourable to passengers, which helped to cease a more pronounced contraction of the market and to delay the need for TAP SA to lower the fares occurred during 2015. Should also be mentioned specific features of the Brazilian market, with potential cash flow impact, such as the practice of instalment sales, as well as agreements, which are regularly established with the acquiring entities, in order to anticipate the receipt TAP SA's receivables.

The American market currently accounts for about 8% of total ticket sales, double the amount it represented in 2013, and equivalent to almost half the current weight of the Brazilian market. The positive exposure to the dollar is important to counterbalance the adverse net exposure to the currency that the TAP Group has in a substantial part of its costs. The perspectives continue to be of growth and expansion in the North American market, which is yet under explored by the TAP Group. The new US routes opened in 2016 began midway through the year and will only have full effect by 2017. On the other hand, new destinations for North America are planned or under analysis, and expansion in the North Atlantic is an element of the new commercial strategy and a source of diversification that is relevant both economically and also in currency exchange terms.

Angola, in 2016, similar to Brazil, registered a sales reduction of close to 20%, accompanied by a very significant reduction in the number of flights, in order to keep flights with a satisfactory load factor and to mitigate problems related to the accumulation of values pending authorization for transfer to Portugal. More than half of the amounts deposited in Angola at the end of 2016 were safeguarded from further currency devaluations, as happened in January 2016, with the acquisition of Angolan treasury bonds indexed to the American dollar.

Other major markets may also be the source of unexpected exchange rate changes, and the United Kingdom was one of those situations in 2016. The pound depreciated by almost 13% in average terms in the year, a depreciation that was inseparable from the referendum about the permanence of the United Kingdom in the European Union in June 2016. It should be noted that TAP SA attempted to counterbalance the devaluation of the pound by the fare adjustment, which meant that, for the year as a whole, the average fares in euro did not reduced.

Despite the strong geographical diversification of the commercial activity and the operational activity of the TAP Group, more than 50% of sales are made in markets whose official currency is the euro, or whose currency has a fixed exchange rate with the euro zone, as is the case of some African countries.

The various foreign exchange costs of the TAP Group are responsible for a significant unbalance in its foreign exchange balance, which is deficient in relation to the US dollar. Generally, the cost headings of the TAP Group are largely dependent on the euro and the dollar, with the remaining currencies, with the exception of the Brazilian real, having a reduced impact. The dollar, however, is the aviation reference currency and covers such diverse and important inputs as fuel, aircraft leasing, maintenance materials and services, aviation insurance, shipping fees and airport charges in many of the geographic areas. Regarding fuel, even in contracts subject to invoicing and settlement in euro, namely in the Portuguese market, the calculation of amounts receivable is indexed, and established by reference, to the quotation of the dollar against the euro, almost total exposure to the dollar, in which only certain commercial rates and fees are excluded, with a marginal weight in the global fuel bill.

Also in the case of operating leases and wet leases the market operates predominantly in dollars from monthly rentals to maintenance reserve costs or to security deposits. Aircraft maintenance is another source of dollar exposure that is not always passed on to the final customer in terms of billing in that currency. The various materials incorporated in the TAP fleet are also normally purchased in dollars. At the strictly financial level, still, since some loans are also denominated in dollars, also the respective interest and capital repayments result in an additional exposure to the American currency. At the end of 2016, 11% of the TAP Group's debt was denominated in dollars, against 13% at the end of 2015.

Exposure to the dollar also has a long-term dimension resulting from the liabilities assumed with the purchase of aircraft in the current framework of investments contracted with Airbus. The order signed with this manufacturer for 53 aircraft to be delivered in the coming years translates into a medium and long-term exposure to the dollar of a very material value related to the final price of the aircraft, in the short term, an annual investment effort of high dollar amounts in the form of pre payments to the manufacturer on account of the ongoing manufacture of the aircraft.

The maintenance company in Brazil is an additional source of foreign exchange risk resulting from the incorporation of several costs in Real, mainly costs with labour. Finally, maintenance and engineering of Brazil is part of the Group's consolidated statement of financial position, so a change in the real at the end of each year generates losses or gains on the equity of the TAP Group. By the end of 2016 the real had appreciated by 20% against the euro compared to the end of 2015. The reverse occurred in 2015, with a devaluation between the end of 2014 and the end of 2015 of 33%. As a result of these changes, equity was subject to an unfavourable adjustment in 2015 and favourable in 2016.

The Group's exposure to currency risk as at 31 December 2016 and 2015, based on its financial position, from financial assets and liabilities converted into euro at the exchange rates at the reporting date, is presented as follows:

	2016					
	USD	BRL	AOA	VEF	OTHER	TOTAL
ASSETS						
Cash and cash equivalents	14,020	1,932	35,584	-	19,766	71,302
Restricted bank deposits (Note 22)	-	-	-	538	-	538
Accounts receivable - customers	19,290	86,656	1,698	24	15,849	123,517
Accounts receivable - other	101,206	45,009	190	-	3,347	149,752
	134,516	**133,597**	**37,472**	**562**	**38,962**	**345,109**
LIABILITIES						
Borrowing (Note 27)	107,292	-	-	-	-	107,292
Accounts payable - suppliers	20,780	15,346	-	162	5,531	41,819
Accounts payable - other	150,001	22,404	1,804	214	6,522	180,945
	278,073	**37,750**	**1,804**	**376**	**12,053**	**330,056**

	2015					
	USD	BRL	AOA	VEF	OTHER	TOTAL
ASSETS						
Cash and cash equivalents	3,814	616	27,286	-	21,403	53,119
Restricted bank deposits (Note 22)	-	-	-	4,177	-	4,177
Accounts receivable - customers	30,385	78,412	1,559	-	13,079	123,435
Accounts receivable - other	72,319	27,979	54	2	458	100,812
	106,518	**107,007**	**28,899**	**4,179**	**34,940**	**281,543**
LIABILITIES						
Borrowing (Note 27)	124,829	13,665	-	-	-	138,494
Accounts payable - suppliers	12,414	23,503	1,810	-	6,072	43,799
Accounts payable - other	120,513	11,963	1,014	76	4,566	138,132
	257,756	**49,131**	**2,824**	**76**	**10,638**	**320,425**

As at 31 December 2016, a 10% variation (positive or negative) of all the exchange rates relative to the Euro, would have an impact in the income statement of some Euro 1,4 million (2014: Euro 4 million).

✈ Interest rate risk

The borrowings of the TAP Group were marginally below Euro 1 billion at the end of 2016, an increase of 5.6% compared to the figure at the end of the year 2015, amounting to Euro 942 million, which in turn had registered a reduction of 11% compared to the figure recorded a year earlier, at the end of 2014, Euro 1,062 million. In terms of net debt, the variations were lower, standing at approximately Euro 845 million at the end of 2016, Euro 805 million at the end of 2015 and Euro 921 million at the end of 2014.

The value of the average debt balance for the year as a whole is more relevant for the purpose of evaluating its cost and impact on the operating results than the balance at the end of each financial year. The average debt for 2016 as a whole was 3% below the average value recorded in 2015.

If by the end of 2015, coinciding with the reprivatisation of the TAP Group, there had been multiple changes in the financial operations in force, including a deep restructuring of short-term debt with national entities, consisting of the conversion of these short-term loans into operations at 7 Years, in 2016 two structuring transactions were executed: the issuance of convertible bonds amounting to Euro 120 million, with a term of 10 years, subscribed in March and June, by Azul SA and Parpública, and the negotiation of a bank loan, with a national institution, collateralised by TAP SA's real estate assets, in the amount of Euro 75 million, with a maturity of 12 years, which began in October. In addition to these operations, the financial activity of the year was normal and the repayment plans in effect for the loans in force were maintained and complied with. For a set of 3 loans with a national entity, an early reimbursement was made, followed by the sales and leaseback of the respective A330 aircrafts, dated 1999.

Despite the contracting of new long-term operations, the share of the short-term portion of total debt increased, as far as a significant number of repayments, negotiated during the reprivatisation process, should be made by the end of 2017, and, consequently were presented as of 31 December 2016, as current borrowing in the statement of financial position. The short-term portion of debt, which had fallen from 60% in 2014 to 21% at the end of 2015, thus increased by the end of 2016 to one third of the total. Following the changes to the prevailing reprivatisation model contained in the Memorandum of Understanding signed by the Group's shareholders, the adjustment to the TAP Group's debt profile is, however, one of the precedent conditions and therefore should be renegotiated with the national financial institutions.

The average cost of the TAP Group's debt decreased in 2016 through interest and exchange rate effects. Total financial costs were reduced from Euro 68 million to Euro 44 million. Of this amount, interest charges decreased moderately from Euro 43 million to Euro 40 million, with the remaining reductions resulting mainly from exchange differences and from other financial expenses. The weighted average interest rate implicit in the 2016 figures, compared to the estimated average debt balance during the year, would have been marginally above 4% and below the same ratio calculated for 2015. The weighted average interest rate, by the end of 2016, however, suffered a worsening compared to the previous year and compared to previous years, due to the higher cost of the new operations. Transactions whose repayments occurred throughout the year had very different fixed or floating rates, so the final interest costs results from the set of fees and spreads weighted by their length of stay and weighted by the corresponding amounts outstanding.

The exchange difference in 2016 was very low compared to the amount recorded in 2015. The dollar debt portion of the TAP Group's total debt is marginally higher than 10% and the appreciation of the US dollar at the end of the year was 10% in 2015 and was only 3% in 2016.

The amount of fixed-rate debt in the total debt remained stable at the end of the year, between 2015 and 2016, approximately 40%. The majority of floating rate loans, corresponding to 60% of the total, bear interests at Euribor, plus the contractual spread, and once more indexed to negative values, for all the terms, during 2016, the amount applied in the respective operations was zero, according to the floor imposed by the financing entities. In practice, all variable-rate euro-denominated credits are charged only to the contractual spread. At the end of 2016, a contractual option was exercised in a long-term credit operation in euro for 6 years, with a floating rate to a fixed rate, with effects on the beginning of 2017.

Interest rate risk has not materialised in recent years, given the long period of rates close to zero that occurred in Europe and also in the United States. However, during 2016 there was a gradual rise in interest rates in dollars and in the end of the year the short and long-term interest rates in this currency increased even more sharply. The future impacts of a rise in the general interest level, either in US Dollar or possibly in Euro, are relevant to the TAP Group, not only in relation to existing debt but possibly more in terms of amounts of debt to be contracted in the future, as a result of the planned investments. Interest rates are also a factor of cost increase in operating leases to be contracted in the future, transactions in which the level of long-term interest rates is normally passed on to the aircraft rental.

As at 31 December 2016 and 2015, financial liabilities with interest rate exposure, by type of interest rate, is as follows:

	2016					
	< 1 year	1 - 2 years	3 - 5 years	6 - 10 years	> 10 years	Total
Variable Rate						
Loans	140,143	-	266,622	142,077	15,000	563,842
Financial leases	34,343	27,213	6,261	137	-	67,954
	174,486	**27,213**	**272,883**	**142,214**	**15,000**	**631,796**
Fixed Rate						
Loans	56,794	7,301	14,878	126,003	-	204,976
Financial leases	96,714	25,151	36,198	-	-	158,063
	153,508	**32,452**	**51,076**	**126,003**	**-**	**363,039**
Total	**327,994**	**59,665**	**323,959**	**268,217**	**15,000**	**994,834**
% fixed rate	**47%**	**54%**	**16%**	**47%**	**0%**	**36%**

	2015					
	< 1 year	1 - 2 years	3 - 5 years	6 - 10 years	> 10 years	Total
Variable Rate						
Loans	21,190	118,659	152,819	172,774	-	465,442
Financial leases	47,873	34,047	33,193	-	-	115,113
	69,063	**152,706**	**186,012**	**172,774**	**-**	**580,555**
Fixed Rate						
Loans	86,943	55,260	22,291	-	-	164,494
Financial leases	42,791	93,398	60,929	-	-	197,118
	129,734	**148,658**	**83,220**	**-**	**-**	**361,612**
Total	**198,797**	**301,364**	**269,232**	**172,774**	**-**	**942,167**
% fixed rate	**65%**	**49%**	**31%**	**0%**	**0%**	**38%**

The TAP Group performs a sensitivity analysis in order to assess the impact in the income statement cause by and increase or decrease in market interest rates, considering all other variables constant. This is an illustrative analysis only, since changes in market rates rarely occur in isolation.

The sensitivity analysis is based on the following assumptions:

- Changes in market interest rates affect interest income and expenses arising from financial instruments subject to floating rates;

✈ Changes in market interest rates only lead to interest income and expenses regarding fixed rate instruments that are measured at their fair value.

Under these assumptions and considering also that: (i) the market interest rate for Euribor is 2% and for dollar Libor is 1.75%, (ii) the Eurodollar exchange rate for 2016 is 1.0541 (2015: 1.0887) and (iii) the intra-annual amortisation is linear for purposes of future interest calculation (simplifying assumption), an increase or decrease of 0.5% in market interest rates, to all currencies in which the Group has loans would have an impact in the future interest expense of some approximately Euro 11 million (2015: Euro 10 million).

Note 27 presents detailed information about the remunerated bank debt financing entity and respective interest rate.

✈ Liquidity risk

The Group's liquidity risk is, therefore, made up of a combination of factors that result from the operation, the existent debt and its repayment schedule, the negotiations conditions for new transactions, the intra-group liquidity, currency conversion gains or losses, and investment activities, when significant. The Group has to ensure, annually, the repayment of its debt, although properly planned and scheduled over time, has an impact on the Group´s treasury and has to be continuously evaluated in accordance with the events occurred during financial years. Any turbulence in financial markets, such as those that occurred during the sovereign debt crisis, or any market changes in terms of the Group current costs or revenues, restricts the treasury, liquidity, economic and financial balance and the prosperity of the Group.

The table below, which includes principal and interests payments, considers assumptions related to market interest rates and Eurodollar exchange, as follows: 2% to Euribor 1.75% to dollar Libor and 1.0541 in Eurodollar (2015: 1.0887 in Eurodollar). The financial liabilities reflect the amounts payable in each maturity, including the estimation of all contractual cash flows including principal and interest payments, not discounted, until borrowings maturity. It was considered a simplifying assumption of linear intra-annual amortisation rate for future interest's calculation purposes:

	2016						
	< 6 months	6 months - 1 year	1 - 2 years	3 - 5 years	6 - 10 years	> 10 years	Total
Loans	48,238	179,975	44,070	340,804	350,476	15,761	979,324
Financial leases	42,787	94,909	55,249	43,738	141	-	236,824
Total	**91,025**	**274,884**	**99,319**	**384,542**	**350,617**	**15,761**	**1,216,148**

	2015						
	< 6 months	6 months - 1 year	1 - 2 years	3 - 5 years	6 - 10 years	> 10 years	Total
Loans	82,450	58,499	202,947	241,542	173,470	-	758,908
Financial leases	57,364	44,954	134,998	98,178	-	-	335,494
Total	**139,814**	**103,453**	**337,945**	**339,720**	**173,470**	**-**	**1,094,402**

✈ Credit Risk

The following table presents elements relative to the Group's assets as at 31 December 2016 and 2015, as well as other accounts receivable, which reflect the credit risk on those dates:

	2016	2015
Non-current assets		
Judicial deposits - Brazil (Note 18)	37,748	24,352
Other non-current assets	83,081	26,600
Current assets		
Cash and cash equivalents	150,468	136,814
Restricted cash	538	4,177
Trade receivables	187,999	138,130
Other current assets	72,431	64,196
	532,265	**394,269**

The Group's quality of credit risk and liquidity, as at 31 December 2016 and 2015, relative to financial assets (cash and cash equivalents and derivative financial instruments), whose counterparts are financial institutions, are detailed as follows:

Rating	2016	2015
AAA	373	-
AA-	286	9
A+	26,077	32
A	2,325	21,587
A-	71	769
BBB+	166	217
BBB	245	4,371
BBB-	1	420
BB+	516	239
BB	-	71
BB-	6,507	898
B+	1,424	47,207
B	538	4,588
B-	71,478	-
CCC+	1,274	-
CCC	-	27,329
Other	39,652	33,160
	150,933	**140,897**
Restricted cash (Note 22)	538	4,177
Bank deposits (Note 22)	150,395	136,720
	150,933	**140,897**

The caption "Other" refers to values related to various international institutions, for which it was not possible to obtain their rating.

As at 31 December 2016 and 2015, the receivables from customers showed the following age structure, considering the maturity date as reference:

	2016	2015
Outstanding values	143,008	106,125
1 to 90 days	19,608	19,355
91 to 180 days	17,750	4,300
181 to 270 days	2,788	529
271 to 365 days	1,502	2,994
over 366 days	82,037	79,619
	266,693	**212,922**
Impairments (Note 21)	(78,694)	(74,792)
Customers - Net value (Note 21)	**187,999**	**138,130**

The values correspond to the amounts owed, after the contracted maturity periods. Although there are delays in the settlement of some values in relation to these maturity periods, this does not result in the identification of impairment losses apart from those considered through the recognised impairment loss. The impairment loss recognised refers, essentially, to debts overdue for more than 366 days.

The balances of airline companies and travel agencies included in Trade receivables, as identified in Note 21, are settled, mainly, through the BSP and the IATA Clearing House system, which substantially reduces the credit risk of the TAP Group.

In addition to short and long term financial management and treasury management, the management of current assets was also closely followed up to monitor customer positions and the impact of the economic crisis on their creditworthiness, and it has been possible to limit the worsening, for example, of adjustments to a value which is not significant for the size of the activity.

✈ Capital management

The Group’s equity shows, synthetically, the evolution of the operating results of the several activities developed by the Group, as well as the accumulated impact of the consecutive transformations on assets and liabilities over time.

The reprivatisation of the TAP Group, completed in November 2015 and approved by ANAC at the end of 2016, created the conditions for the entry of private contributions. A substantial part of this investment was still in 2015 in the form of supplementary capital contributions and, as defined in the agreement between the Portuguese State and Atlantic Gateway, the private investors would subsequently have to make quarterly capital inflows throughout 2016, amounting to some Euro 70 million.

Following the reinforcement of own funds in 2015 and 2016, TAP Group's equity stood at a negative amount of Euro 470 million at the end of 2016, against a negative Euro 530 million at the end of 2015. While the final value reached in 2015 despite the entry of supplementary capital contributions, was negatively affected by the loss of Euro 91 million in connection with the devaluation of TAP SA's funds retained in Venezuela, the improvement in 2016 resulted from the combined positive and negative effects of entry of supplementary capital contributions and operating results, namely the negative holding result of the maintenance company in Brazil and, on the other hand, the positive impact on the Group's accounts of the appreciation of the Brazilian unit, due to the appreciation of the Brazilian real.

Total assets recorded a significant increase highlighting the variations related to cash and cash equivalents, tangible fixed assets and trade receivables. The treasury had a positive impact on the balance of bank deposits, joint with the amount invested in sovereign bonds in Angola, indexed to the US dollar, which will allow the safeguarding of the deposits previously denominated in Kwanzas for a total amount of some Euro 40 million.

The substantial increase in tangible fixed assets of Euro 78 million, net of depreciation of Euro 57 million, essentially relates to the pre delivery payments made to Airbus in accordance with the aircraft purchase agreement in place. A smaller portion of the increase in tangible fixed assets is related to ongoing investments in the current fleet, which will continue to increase as the existing aircraft renewal program continues its implementation.

Also highlighted in the statement of financial position was the amount corresponding to the assets of the subsidiary LFP, for which the TAP Group agreed the selling of 51% of the subsidiary shares with Vinci Airports in 2016.

In liabilities, there were increases in balances of other payables, although the balance of suppliers debt, in particular, fell by around 10% in 2016. There was a significant increase in the liabilities from unused flight documents, corresponding to an increase in sales, not yet "flown", by TAP SA.

It was also evidenced the amount of the liability of the subsidiary LFP, as a result of the commitment, mentioned above, to sell the free shop operation.

Regarding borrowings, although it decreased in average terms for the year as a whole, it increased by 5.6% at the end of 2016 compared to 2015, standing at around Euro 1 billion. The TAP Group's debt has a strict accounting policy but can be analysed and measured in a more extensive and substantial way, aggregating liabilities that, in some aspects, are similar to borrowings, although in the form of operating leases. The increase in the set of aircraft operating lease costs corresponds to an increase in significant future liabilities, as far as these are medium and long-term contracts, which are close to staggered debt payments, although there is no risk of residual value of the aircraft at the end of the lease. In addition to the renewal of the regional fleet, already completed in 2016, and the capacity expansion, carried out in 2016 and in previous years, will be relevant for risk management, and for the return on invested capital, the future increase of debt that may occur in the form of borrowing, or in the form of an operating lease, to enable the investment cycle in the Group's new fleet in the coming years.

4 - Employees

During 2016 and 2015, the average number of employees working for TAP SGPS and all its subsidiaries was 11,019 and 11,023, respectively.

	2016				
	Air Transport	Maintenance	Catering	Other	Total
Portugal	5,027	1,906	487	1,234	8,654
Brazil	129	1,870	-	-	1,999
Other	362	4	-	-	366
	5,518	**3,780**	**487**	**1,234**	**11,019**

	2015				
	Air Transport	Maintenance	Catering	Other	Total
Portugal	5,053	1,881	501	1,187	8,622
Brazil	129	1,892	-	-	2,021
Other	375	5	-	-	380
	5,557	**3,778**	**501**	**1,187**	**11,023**

5 - Tangible fixed assets

During the years ended 31 December 2016 and 2015, changes in tangible fixed assets, as well as the accumulated depreciation and impairments losses, were as follows:

	2016									
	Land and natural resources	Buildings and other constructions	Basic equipment	Transport equipment	Tools and utensils	Administrative equipment	Other tangible fixed assets	Other assets in progress	Advances to suppliers of tangible assets	**Total**
Acquisition Cost										
Opening balance	41,674	347,081	1,921,837	5,671	30,905	65,369	26,960	7,678	49,867	**2,497,042**
Additions	-	253	34,384	969	2,134	1,111	1,723	15,537	120,309	**176,420**
Disposal	-	-	(156,748)	(52)	(2)	(20)	-	-	-	**(156,822)**
Other transfers / write-offs	-	-	(3,038)	(290)	582	(471)	(22)	(595)	(3,384)	**(7,218)**
Currency conversion differences	130	814	2,757	18	2,143	752	-	519	-	**7,133**
Transfer to non-current assets held for sale (Note 23)	-	-	(574)	(61)	(33)	(2,564)	(16,813)	-	-	**(20,045)**
Closing balance	**41,804**	**348,148**	**1,798,618**	**6,255**	**35,729**	**64,177**	**11,848**	**23,139**	**166,792**	**2,496,510**
Accumulated Depreciation										
Opening balance	-	252,634	1,495,358	5,318	21,173	63,045	18,513	-	-	**1,856,041**
Depreciation for the year (Note 50)	-	5,689	46,513	296	887	1,079	210	-	-	**54,674**
Impairment losses recognized	-	-	2,294	-	-	-	-	-	-	**2,294**
Disposal	-	-	(127,602)	(52)	(2)	(20)	-	-	-	**(127,676)**
Other transfers / write-offs	-	-	(1,463)	(290)	(21)	(475)	19	-	-	**(2,230)**
Currency translation differences	-	362	2,407	17	1,296	709	-	-	-	**4,791**
Transfer to non-current assets held for sale (Note 23)	-	-	(527)	(51)	(27)	(1,657)	(8,085)	-	-	**(10,347)**
Closing balance	**-**	**258,685**	**1,416,980**	**5,238**	**23,306**	**62,681**	**10,657**	**-**	**-**	**1,777,547**
Carrying Amount	**41,804**	**89,463**	**381,638**	**1,017**	**12,423**	**1,496**	**1,191**	**23,139**	**166,792**	**718,963**

	2015									
	Land and natural resources	Buildings and other constructions	Basic equipment	Transport equipment	Tools and utensils	Administrative equipment	Other tangible fixed assets	Other assets in progress	Advances to suppliers of tangible assets	**Total**
Acquisition Cost										
Opening balance	41,916	349,154	2,093,064	5,662	33,009	67,322	23,689	3,332	17,167	**2,634,315**
Additions	-	-	9,513	90	565	697	7,606	5,637	32,700	**56,808**
Disposal	-	-	(164,566)	-	(10)	-	-	-	-	**(164,576)**
Other transfers / write-offs	(71)	(999)	(12,401)	(58)	54	(1,676)	(4,335)	(659)	-	**(20,145)**
Currency conversion differences	(171)	(1,074)	(3,773)	(23)	(2,713)	(974)	-	(632)	-	**(9,360)**
Closing balance	**41,674**	**347,081**	**1,921,837**	**5,671**	**30,905**	**65,369**	**26,960**	**7,678**	**49,867**	**2,497,042**
Accumulated Depreciation										
Opening balance	-	248,033	1,598,925	5,229	22,020	64,270	22,120	-	-	**1,960,597**
Depreciation for the year (Note 50)	-	5,748	53,436	166	998	1,062	191	-	-	**61,601**
Depreciation from discontinued operations (Note 23)	-	-	18	2	-	277	537	-	-	**834**
Disposal	-	-	(143,580)	-	(5)	-	-	-	-	**(143,585)**
Other transfers / write-offs	-	(710)	(10,071)	(57)	(207)	(1,653)	(4,335)	-	-	**(17,033)**
Currency translation differences	-	(437)	(3,370)	(22)	(1,633)	(911)	-	-	-	**(6,373)**
Closing balance	**-**	**252,634**	**1,495,358**	**5,318**	**21,173**	**63,045**	**18,513**	**-**	**-**	**1,856,041**
Carrying Amount	**41,674**	**94,447**	**426,479**	**353**	**9,732**	**2,324**	**8,447**	**7,678**	**49,867**	**641,001**

The land, buildings and other constructions of the head office of TAP S.A. were transferred to this subsidiary's ownership under Decree-Law number 351/89 of 13 October.

The main impacts occurred during the year ended 31 December 2016 are as follows:

- The additions of basic equipment in the amount of Euro 34,384 thousand, essentially refers to: (i) investment in fleet equipment, namely the introduction of sharklet technology in the aircrafts in the amount of Euro 4,806 thousand, cabin retrofit in the amount of Euro 7,501 thousand and the amount of Euro 6,500 thousand related to the useful life extension of the A319/A320/A321 fleets (Extended Service Goal - ESG) and (ii) capitalisation of expenses with structural aircraft maintenance for own aircrafts or acquired through financial leasing arrangements in the amount of Euro 10,339 thousand.

- The increase recorded in the heading "Advances to suppliers of tangible fixed assets", in the amount of Euro 120,309 thousand, refers, essentially, to the pre delivery payments made for future aircrafts acquisition (Note 60).

- The additions of other assets in progress, in the amount of Euro 15,537 thousand, refers essentially to the consulting services provided in the process of negotiating purchase agreements for future aircraft acquisition (Note 60) in the amount of Euro 4,595 thousand and to the cabin retrofit project, in the amount of Euro 7,686 thousand.

- Basic equipment disposals, in the net amount of Euro 29,146 thousand, mostly relate to the sale of three A330 aircraft, due to a sales and leaseback operation, which resulted in a gain of Euro 16,261 thousand (Note 48).

- Transfers to non-current assets held for sale relate to the tangible fixed assets of the subsidiary LFP

The main impacts occurred during the year ended 31 December 2015 are as follows:

- The additions of basic equipment in the amount of Euro 9,513 thousand, essentially refers to: (i) spare parts in the amount of Euro 9,513 thousand; (ii) a communication system project (FANS B+) related to fleet and aircraft equipment in the amount of Euro 2 million; (iii) aircraft maintenance material in the amount of Euro 1,4 million; and (iv) information technology equipment in the amount of Euro 1 million.

- The additions of other tangible fixed assets, in the amount of Euro 7,606 thousand, refers, mainly, to refurbishment carried out in Free Shop stores at the airports of Lisbon and Oporto.

- The increase in the heading "Advances to suppliers of tangible assets", in the amount of Euro 32,700 thousand, refers, essentially, to the pre delivery payments made for future aircraft acquisition, in the amount of Euro 27,271 thousand (Note 60), added to the amount of Euro 5,429 thousand related to the introduction of sharklet technology in the aircrafts and to the useful life extension of the A319/A320/A321 fleets (ESG).

- Moreover, the additions of other assets in progress, in the amount of Euro 5,637 thousand refers to consulting services provided in the process of negotiating purchase agreements for future aircraft acquisition (Note 60).

- Basic equipment disposals, in the net amount of Euro 20,986 thousand, refers, essentially, to the disposal of 6 aircraft A319, due to a sale and leaseback operation, which resulted in a gain of some Euro 24,207 thousand (Note 48).

- Transfers and write-offs of basic equipment refer, essentially, to the write-off of spare parts as scrap and other miscellaneous maintenance equipment.

As at 31 December 2016 and 2015, the heading "Basic equipment" is detailed as follows:

	2016			**2015**		
	Acquisition cost	Accumulated depreciation	Carrying amount	Acquisition cost	Accumulated depreciation	Carrying amount
Flight equipment						
Aircraft	439,276	(384,828)	54,448	380,141	(349,610)	30,531
Spare engines	22,754	(17,211)	5,543	24,369	(17,932)	6,437
Spare parts	118,833	(86,606)	32,227	118,109	(85,162)	32,947
	580,863	(488,645)	92,218	522,619	(452,704)	69,915
Flight equipment under financial leases						
Aircraft	1,101,841	(830,394)	271,447	1,284,858	(947,300)	337,558
	1,101,841	(830,394)	271,447	1,284,858	(947,300)	337,558
Machines and miscellaneous equipment	115,914	(97,941)	17,973	114,360	(95,354)	19,006
	1,798,618	**(1,416,980)**	**381,638**	**1,921,837**	**(1,495,358)**	**426,479**

As at 31 December 2016 and 2015, the Group's aircraft fleet is detailed as follows:

	2016				2015			
	Owned by TAP Group	Finance leases	Operating leases	Total	Owned by TAP Group	Finance leases	Operating leases	Total
Airbus A340	4	-	-	**4**	4	-	-	**4**
Airbus A330	-	8	8	**16**	-	11	3	**14**
Airbus A319	-	9	12	**21**	-	9	12	**21**
Airbus A320	1	4	14	**19**	-	5	14	**19**
Airbus A321	-	2	1	**3**	-	2	1	**3**
Fokker 100	-	6	-	**6**	-	6	-	**6**
Embraer 145	-	8	-	**8**	-	8	-	**8**
Embraer 190	**-**	**-**	**9**	**9**	**-**	**-**	**-**	**-**
	5	**37**	**44**	**86**	**4**	**41**	**30**	**75**

In the scope of the regional operation, the TAP Group created a new image and commercial brand - TAP Express - to be used in aircrafts operated by Portugália and White, companies with which TAP SA celebrated ACMI contracts, (Aircraft, Crew, Maintenance and Insurance).

In July 2016, eight ATR 72-600 aircrafts operated by White, mainly used in the Lisbon / Oporto air-bridge, started operation.

In October 2016, nine Embraer E190 aircrafts, operated by Portugália, mainly used on the nearest and with lowest density European routes, were also incorporated in the operation.

During the year 2015 the TAP Group used two ATR 42-600 aircrafts from White, which were being operated by TAP, S.A. under an ACMI agreement.

To guarantee payment of the amounts due under a loan agreement with a national institution, in the amount of Euro 75 million, a mortgage was set up on an urban building of TAP SA, composed by twenty-nine office buildings, workshops for construction materials and others, located at the Lisbon Airport (Note 27).

Depreciation of tangible fixed assets is recognised under "Depreciation and amortisation costs" in the consolidated income statement (Note 50).

6 - Investment properties

As at 31 December 2016, "Investment properties" refers to: i) a property in Maputo (Mozambique); ii) two apartments in Sacavém, and iii) an apartment in Oporto which was transferred, in 2015, from the caption tangible fixed assets according to its undetermined use.

The movement occurred in this caption was as follows:

	2015	2015
Opening balance	2,216	2,139
Fair value adjustments - net gains and losses (Note 47)	32	(174)
Transfers	-	251
Closing balance	**2,248**	**2,216**

The fair value of the investment properties was determined by an independent expert with recognised professional qualifications, where the methods and significant assumptions applied in the determination of the fair value of the properties was supported by market evidence.

The amounts recognised through profit or loss for the year, related to income from rents and direct operating costs, are immaterial in the Group's financial statements as a whole.

7 - *Goodwill*

During 2016 and 2015, the movement was as follows:

	2016		
	Opening balance	Currency translation differences	Closing balance
Air Transport	63,099	-	63,099
Maintenance and Engineering Brazil	86,692	22,269	108,961
	149,791	**22,269**	**172,060**

	2015		
	Opening balance	Currency translation differences	Closing balance
Air Transport	63,099	-	63,099
Maintenance and Engineering Brazil	130,380	(43,688)	86,692
	193,479	**(43,688)**	**149,791**

The positive amount of Euro 22,269 thousand refers to the currency translation differences of the Goodwill of Maintenance and Engineering Brazil, which is denominated in Brazilian Real in the amount of Real 373,791,337.

It should be noted that, from the amount recorded in the previous year, approximately Euro 14.5 million are related to prior years, due to the fact that foreign currency translation reserves have been properly recorded in year ended on 31 December 2015, at the level of functional currency of the operations acquired in Brazil and not at the level of the acquired legal entity. This amount is considered to be insignificant in the context of the financial position of TAP Group.

Accordingly to IAS 36, goodwill is subject to impairment tests carried out on an annual basis, as described in the accounting policy (Note 2.9).

Goodwill is attributed to the Group's cash-generating units (CGUs), identified in accordance with the business segment and country of the operation, as follows:

	2016		
	Air Transport	**Maintenance**	**Total**
Portugal	63,099	-	63,099
Brazil	-	108,961	108,961
	63,099	**108,961**	**172,060**

	2015		
	Air Transport	**Maintenance**	**Total**
Portugal	63,099	-	63,099
Brazil	-	86,692	86,692
	63,099	**86,692**	**149,791**

For the purposes of impairment tests, the recoverable value of the CGUs is determined based on the value in use, in accordance with the discounted cash flow method. The calculations are based on historical performance and expectations of business development with the current productive structure, considering the budget for the following year and an estimation of cash flows for the subsequent 4 years.

For the Maintenance and Engineering Brazil business unit, was considered a budget for the following year and an estimation of cash flows for the subsequent period of 7 years which incorporated, namely, the recovery of the existent tax losses.

As a result of the impairment tests conducted to the different CGUs, no impairment losses on goodwill were identified.

The main assumptions used for the purposes of impairment tests were the following:

31 December 2016	**Portugal**	**Brasil**
Discount rate*	8.9%	14.5%
CAGR of revenue**	7.7%	14.4%
Perpetuity growth	2.0%	5.0%
Tax rate	25.5%	34.0%

31 December 2015	**Portugal**	**Brasil**
Discount rate*	8.9%	16.5%
CAGR of revenue**	4.1%	15.2%
Perpetuity growth	2.0%	5.0%
Tax rate	25.5%	34.0%

* Discount rate net of taxes

** *Compound Annual Growth Rate* of revenue - year-on-year growth rate of na investment over a given period of time

The impairment tests carried out in 2016 sustain the recoverability of the book value of the referred cash-generating units. As at 31 December 2016, the book value of the air transport unit stands at Euro 207,731 thousand (2015: Euro 181,271 thousand), and the book value of the maintenance unit in Brazil is negative by Euro 283,529 thousand (2015: negative by Euro 191,710 thousand).

8 - Other intangible assets

During 2016 and 2015, changes in other intangible assets were as follows:

	Industrial property and other rights	Computer programmes	Assets in progress	Total
Acquisition cost				
Balance as at 1 January 2015	**11,952**	**2,780**	**-**	**14,732**
Additions	-	75	5	80
Currency translation differences	-	(30)	-	(30)
Balance as at 31 December 2015	**11,952**	**2,825**	**5**	**14,782**
Acquisitions	-	1,268		1,268
Regularisation, transfer and write-off	-	(16)	(5)	(21)
Currency conversion differences	-	23	-	23
Transfer to Assets Held for Sale (Note 23)	-	(723)	-	(723)
Balance as at 31 December 2016	**11,952**	**3,377**	**-**	**15,329**
Accumulated amort. and impairment losses				
Balance as at 1 January 2015	**(11,952)**	**(2,042)**	**-**	**(13,994)**
Amortisations and impairment losses (Note 50)	-	(250)	-	(250)
Amortisation from discontinued operations (Note 23)	-	(12)	-	(12)
Currency translation differences	-	8	-	8
Balance as at 31 December 2015	**(11,952)**	**(2,296)**	**-**	**(14,248)**
Amortisations and impairment losses (Note 50)	-	(228)	-	(228)
Currency translation differences	-	(11)	-	(11)
Transfer to non-current assets held for sale (Note 23)	-	662		662
Balance as at 31 December 2016	**(11,952)**	**(1,873)**	**-**	**(13,825)**
Carrying amount as at 31 December 2015	**-**	**529**	**-**	**534**
Carrying amount as at 31 December 2016	**-**	**1,504**	**-**	**1,504**

10 – Investment in associates

As at 31 December 2016 and 2015, the investment in SPdH is reduced to zero and the liabilities attributable to the TAP Group are recorded in provisions (see "Provisions for financial investments" in Note 26).

13 - Other financial assets

As at 31 December 2016 and 2015, other financial non-current assets are detailed as follows:

	2016	2015
Angola's treasury bonds	39,654	-
Bank deposits in Guinea Bissau	1,813	1,838
SITA Group Foundation	648	648
Salvor Hotéis Moçambique loan	61	255
Other	211	212
Impairment losses	(1,827)	(1,853)
	40,560	**1,100**

During 2016, Angola's Treasury bonds were subscribed for a total amount of Kwanza 6,899,934 thousand (Euro 39,654 thousand), corresponding to the original exchange rate of 165,074 kwanzas per dollar. These bonds have a maturity date of 6 December 2018 and are indexed to the US dollar.

During 2014, the existent cash and cash equivalents at “Banco Internacional da Guiné Bissau” were considered as non-recoverable following the dissolution and liquidation of this institution, and thus impairment loss for the total amount was recognised.

The value presented for the SITA Group Foundation refers essentially to 519,778 certificates (unlisted securities) of that company, which was founded by Société International de Télécommunications Aéronautiques.

The movement which occurred in this heading during 2016 and 2015 was as follows:

	2016	2015
Opening balance	1,100	2,122
Increases	39,654	-
Decreases	(198)	(1,128)
Currency translation differences	2	98
Other movements	2	8
Closing balance	**40,560**	**1,100**

15 - Deferred tax assets and liabilities

As mentioned in Note 2.14, the Group recorded deferred taxes related to the temporary differences between assets and liabilities for tax and accounting purposes, as well as existing tax losses carried forward as at the date of the consolidated statement of financial position.

The Group believes that the deferred tax assets recognised in the consolidated statement of financial position are recoverable, both through their use in reducing future taxable profits, based on the net income of TAP S.A. budgeted for 2017 on net income projections for subsequent years, adjusted by differences between the accounting and tax results, and through the reversal of deferred tax liabilities.

As at 31 December 2016 and 2015 the tax rate used to calculate the deferred tax assets relating to tax losses carried forward was 21%. In the case of temporary differences, the rate used was 27.5%, when it was deemed that the taxation of temporary differences in the estimated period of application of the aforesaid rate was probable.

Tax benefits are considered at 100%, whereas, in some cases, their full acceptance is still dependent on the approval of the authorities granting these tax benefits. The deferred taxes arising from tax benefits are recorded when they have been approved by the authorities granting these tax benefits.

The main temporary differences between accounting and taxable amounts as at 31 December 2016 and 2015, the corresponding deferred tax assets and liabilities and the respective effect on the results for 2016 and 2015 are as follows:

	2016				
	Opening balance	Effect in results (Note 52)	Effect in comprehensive income	Transfer to assets held for Sale (Note 23)	Closing balance
Deferred tax assets					
Tax losses carried forward	38,050	(2,589)	-	-	35,461
Employee benefits obligations	13,935	(954)	2,172	-	15,153
Impairment losses in inventories	8,155	305	-	-	8,460
Impairment losses in fixed assets	506	585	-	-	1,091
Impairment losses of accounts receivable	7,481	(519)	-	-	6,962
Derivative financial instruments (Note 24)	286	-	(111)	-	175
Tax benefits	517	(381)	-	-	136
Other provisions and adjustments not accepted for tax purposes	555	(264)	-	(158)	133
	69,485	**(3,817)**	**2,061**	**(158)**	**67,571**
Deferred tax liabilities					
Revaluation of tangible fixed assets	20,037	(615)	-	-	19,422
	20,037	**(615)**	**-**	**-**	**19,422**
		(3,202)	**2,061**		

	2015				
	Opening balance	Effect in results (Note 52)	Effect in comprehensive income	Movements related to discontinued operations (Note 23)	Closing balance
Deferred tax assets					
Tax losses carried forward	8,572	29,478	-	-	38,050
Employee benefits obligations	14,155	(1,032)	812	-	13,935
Impairment losses in inventories	8,052	103	-	-	8,155
Impairment losses in fixed assets	506	-	-	-	506
Impairment losses of accounts receivable	6,336	1,145	-	-	7,481
Derivative financial instruments (Note 24)	13,931	-	(13,645)	-	286
Tax benefits	1,387	(870)	-	-	517
Other provisions and adjustments not accepted for tax purposes	471	89	-	(5)	555
	53,410	**28,913**	**(12,833)**	**(5)**	**69,485**
Deferred tax liabilities					
Revaluation of tangible fixed assets	21,035	(998)	-	-	20,037
	21,035	**(998)**	**-**	**-**	**20,037**
		29,911	**(12,833)**		

✈ Tax losses carried forward

Under the terms of current tax legislation in Portugal, tax losses generated as of 2014 can be carried forward for a period of twelve years after their occurrence and may thus be deducted to taxable profits generated over this period, up to the limit of 70% of the taxable profit in the following years.

In Brazil, tax losses have not a limited period for its deduction. However, the deduction is limited to 30% of taxable profit for the following years.

The Group considers that, as at 31 December 2016, tax losses carried forward by TAP S.A. are recoverable, through their use in the reduction of future taxable profit, and therefore recorded the corresponding deferred tax assets.

The tax losses carried forward as at 31 December 2016 and used in 2016 are detailed as follows:

1 January 2016	2012	2013	2014	2015	2016	Total
TAP SGPS	2,923	-	3,549	2,138	n/a	**8,610**
TAP S.A.	-	-	71,617	208,529	n/a	**280,146**
Portugália	-	-	-	33	n/a	**33**
UCS	251	95	-	-	n/a	**346**
TAP M&E Brasil	24,972	19,911	51,225	9,464	n/a	**105,572**
	28,146	**20,006**	**126,391**	**220,164**	**n/a**	**394,707**

Use in 2016	2012	2013	2014	2015	2016	Total
TAP SGPS	-	-	-	-	n/a	**-**
TAP S.A.	-	-	(12,285)	-	n/a	**(12,285)**
Portugália	-	-	-	(33)	n/a	**(33)**
UCS	(9)	-	-	-	n/a	**(9)**
TAP M&E Brasil	-	-	-	-	n/a	**-**
	(9)	**-**	**(12,285)**	**(33)**	**n/a**	**(12,327)**

31 December 2016	2012	2013	2014	2015	2016 Estimated	Total
TAP SGPS	2,923	-	3,549	2,138	821	**9,431**
TAP S.A.	-	-	59,332	208,529	-	**267,861**
Portugália	-	-	-	-	-	**-**
UCS	242	95	-	-	-	**337**
TAP M&E Brasil	24,972	19,911	51,225	9,464	11,512	**117,084**
	28,137	**20,006**	**114,106**	**220,131**	**12,333**	**394,713**
Limit for deduction (in Portugal)	**2017**	**2018**	**2026**	**2027**	**2028**	

16 - Advances to suppliers

The advances to suppliers as at 31 December 2016 and 2015 refer to the following entities:

	2016	2015
Eagle Services Asia	3,767	-
SITA	635	615
Sr Technics Sw itzerland, Ltd.	-	689
Others	5,481	3,240
	9,883	**4,544**

17 - State and other public entities

The balances with the State and other public entities are detailed as follows:

	2016	2015
Current assets		
Income tax receivable	10,473	4,268
Other	12,512	13,159
	22,985	**17,427**
Current liabilities		
Other	35,452	22,468
	35,452	**22,468**

The amounts relative to 2016 and 2015 are detailed as follows:

	2016		2015	
	Assets	Liabilities	Assets	Liabilities
State - Grants receivable:				
Fare Compensation	1,473	-	1,354	-
State and Other Public Entities:				
Income Tax	10,473	-	4,268	-
Income Tax - Withholdings made to third	-	103	-	2,580
Income tax - Withholdings made to third		-	16,031	-	8,802
VAT	6,429	987	7,840	366
Social Security	-	16,726	-	9,611
State - Brazil	4,588	1,381	3,918	810
Other	22	224	47	299
	22,985	**35,452**	**17,427**	**22,468**

As at 31 December 2016 and 2015, the value recorded under the heading "Fare Compensation" includes the part of the fare subsidised by the Portuguese State for the routes of the Autonomous Region of the Azores until 29 March 2015, in the total amount of 516 thousand euros and 450 thousand euros, respectively. These values correspond to tickets sold by “TAP S.A.” which may be used on “TAP S.A.” or other airline flights. This caption also includes receivable amount from the Portuguese State of 958 thousand euros and 904 thousand euros, respectively, relative to flights between the islands of the Autonomous Region of the Azores. The figures for the second semester of 2014 and the years of 2015 and 2016 have not yet been verified and audited by the Portuguese Authorities or approved by the Government. However, no significant corrections to the values recorded by the Group are expected.

The Group recognises, annually, under the caption Sales and services rendered, grants receivable from the Portuguese State which reimburses the fare of the ticket for passengers to or from the Azores, since passengers are covered by the applicable legal regime. The amount recognised each year corresponds to the Group's estimation for the amount receivable for tickets flown by those passengers. It should be noted that, due to liberalization of Azores airspace, with effects from 29 March 2015, on the responsibility of reimbursement request was transferred to the passengers.

As at 31 December 2016, the VAT receivable refers, essentially, to reimbursement requests, which have not yet been received, relative to the months of November and December 2016.

Decree-Law nº 258/98 of 17 August repealed the tax exemptions from which "TAP S.A." had benefited, and which had been established based on XII attached to Decree-Law nº 39.188 of 25 April 1953 and on Decree-Law nº 39.673 of 22 May 1954, nº 41.000 of 12 February 1957 and nº 44.373 of 29 May 1962, which implied that "TAP S.A." is no longer exempt from the payment of tax and other contributions to the State.

18 - Other receivables

As at 31 December 2016 and 2015, other receivables is detailed as follows:

	2016		2015	
	Current	Non-current	Current	Non-current
Related parties (Note 56)	1,263	9,444	106	4,700
Personnel	14,572	-	12,159	-
Accrued income	15,048	-	14,405	-
Other	36,294	72,746	37,570	47,073
Impairment losses of other receivables	(4,629)	(1,921)	(4,588)	(1,921)
	62,548	**80,269**	**59,652**	**49,852**

✈ **Related parties - non-current**

As at 31 December 2016, the caption "Related parties - non-current" includes: (i) the amount of Euro 4,700 thousand, relating to the supplementary capital contribution granted to SPdH (Notes 26 and 56), and (ii) Euro 4,744 thousand related to security deposits provided to Azul S.A. (Notes 27 and 56).

✈ Accrued income

As at 31 December 2016 and 2015, the amount recorded under the caption "Accrued income" is detailed as follows:

	2016	2015
Work for aviation companies	11,574	7,289
Sale of miles to partners	1,235	1,889
Advertising	-	4,173
Other	2,239	1,054
	15,048	**14,405**

As of 31 December 2015, the increase in accrued income from advertising refers to the subsidiary L.F.P. - Lojas Francas de Portugal, S.A., which is classified as held for sale on 31 December 2016 (Note 23).

✈ Other – non-current

As at 31 December 2016 and 2015, the amount recorded under the caption "Other - non-current" corresponds to:

	2016	2015
Judicial deposits - Brazil	37,748	24,352
Security deposits (Note 27)	25,006	12,954
SITA - Société Internationale de Télécommunications Aéronautiques	315	335
Other	9,677	9,432
	72,746	**47,073**

The caption “Judicial deposits – Brazil” refers to security deposits related to several labour, fiscal and civil legal processes in which TAP M&E Brasil is involved (Note 26). The increase refers, mainly, to the effect of the foreign currency exchange of the Brazilian real.

The security deposits are constituted under the operating lease contracts for aircraft and engines, and will be returned, without interests, when the aircraft and engines are returned to their lessors. The increase verified is related to the guarantee deposits associated with the new operating lease contracts carried out in 2016.

✈ **Other - current**

As at 31 December 2016 and 2015, the amount recorded under the caption "Other - current" corresponds to:

	2016	2015
Interline and other invoicing	10,248	11,439
Receivables from suppliers	6,446	7,132
Pasogal SGPS, S.A. (Note 37)	3,000	3,000
VAT of Representations	2,476	3,265
Debtors - Brazil	2,246	3,315
Deposits and guarantees	1,558	955
Debtors - Italy	745	595
Other	9,575	7,869
	36,294	**37,570**

The caption "Other", in the amount of Euro 9,575 thousand, includes Euro 531 thousand relative to the financing surplus (2015: Euro 637 thousand), recorded as at 31 December 2016, of the “Horizonte Valorização” Pension Fund of the subsidiary UCS. This financing surplus is reimbursable under the terms of the law and/or exemption from future contributions (Note 28).

✈ **Impairment losses on other receivables**

The movement which occurred in this caption during 2016 and 2015 is as follows:

Opening balance as at 1 January 2015	**6,401**
Increases (Note 44)	143
Reversals (Note 44)	(33)
Utilisation	(2)
Closing balance as at 31 December 2015	**6,509**
Increases (Note 44)	73
Reversals (Note 44)	(30)
Utilisation	(2)
Closing balance as at 31 December 2016	**6,550**

19 – Deferrals

As at 31 December 2016 and 2015, the caption "Deferrals" is detailed as follows:

	2016	2015
Deferred costs	17,296	13,272
	17,296	**13,272**

	2016	2015
Deferred incomes	68,040	64,129
	68,040	**64,129**

The amount recorded under the caption "Deferred costs", as at 31 December 2016 and 2015, is detailed as follows:

	2016	2015
Rental costs	5,414	2,953
Aircraft and engine leases	4,791	4,866
Commissions	2,722	1,906
Related entities (Note 56)	731	-
Insurance	446	1,659
Equipment maintenance	384	316
Other deferred costs	2,808	1,572
	17,296	**13,272**

Commissions refer to the values paid to agents for tickets sold but which have not yet been used and have not expired until 31 December 2016 and 2015.

The caption "Deferred income", as at 31 December 2016 and 2015, is detailed as follows:

	2016	2015
Customer loyalty programme	42,972	41,995
Work for aviation companies	22,227	20,686
Other	2,841	1,448
	68,040	**64,129**

Under the application of IFRIC 13 - Customer loyalty programme, the attribution of miles to customers who are members of the "TAP Victoria" customer loyalty programme is deferred based on the unit value of the mile, as perceived by the customer (Note 2.27).

The amount of Euro 22,227 thousand (2015: Euro 20,686 thousand), recorded under the caption "Work for aviation companies", refers to advanced billing of maintenance work for third parties that was in progress as at 31 December 2016.

20 - Inventories

On 31 December 2016 and 2015, the detail of the inventories is as follows:

	2016	2015
Goods (Note 40)	64	16,719
Products and w ork in progress (Note 38)	7,870	5,545
Raw materials, inputs and consumables (Note 40)	127,001	108,125
Inventory impairment losses	(49,096)	(44,355)
	85,839	**86,034**

As of 31 December 2015, the caption of Goods refers essentially to the subsidiary LFP, which is classified as held for sale on 31 December 2016 (Note 23), justifying the variation occurred.

The caption "Products and work in progress" corresponds to the value of materials and hours spent on aircraft maintenance works for third parties which are still in progress at the reporting date.

“Raw, materials, inputs and consumables” refer, essentially, to technical material used in aircraft maintenance services for the Group’s fleet and for third parties. The variation occurred is essentially due to the exchange rate effect arising from the appreciation of the real against the euro.

The movement of Inventory impairment losses in 2016 and 2015 is as follows:

Opening balance as at 1 January 2015	**49,432**
Increases (Note 43)	533
Increases from discontinued operations (Note 23)	58
Reversals (Note 43)	(739)
Utilisation	(58)
Currency conversion differences	(4,871)
Closing balance as at 31 December 2015	**44,355**
Increases (Note 43)	2,643
Reversals (Note 43)	(831)
Utilisation	(13)
Currency conversion differences	3,671
Transfer to non-current assets held for sale (Note 23)	(729)
Closing balance as at 31 December 2016	**49,096**

The currency translation differences verified in 2016 and 2015 arises from the conversion of the Brazilian subsidiary financial statements.

21 – Trade receivables

As at 31 December 2016 and 2015, the caption "Trade receivables" is detailed as follows:

	2016	**2015**
Trade receivables - current account	211,160	173,215
Trade receivables - doubtful accounts	55,533	39,707
Impairment of trade receivables	(78,694)	(74,792)
	187,999	**138,130**

The detail of this heading by type of customer is as follows:

	2016	**2015**
Travel agencies	93,083	59,554
Private entities	61,045	48,076
Airline companies	28,371	21,855
Related parties (Note 56)	2,165	1,157
Other	3,335	7,488
	187,999	**138,130**

The increase in private entities is mainly due to the increase in ticket sales in the last months of 2016, when compared to the same period of the previous year, as well as to the exchange rate effect resulting from the appreciation of the real against the euro.

The trade receivable from travel agencies and airline companies are primarily settled through IATA Billing and Settlement Plan (BSP) and IATA Clearing House (ICH).

The movement of "Impairment of trade receivables" in 2016 and 2015 is as follows:

Opening balance as at 1 January 2015	**72,842**
Increases (Note 44)	6,908
Increases from discontinued operations (Note 23)	17
Reversals (Note 44)	(1,363)
Utilisation	(510)
Currency translation differences	(3,102)
Closing balance as at 31 December 2015	**74,792**
Increases (Note 44)	4,485
Reversals (Note 44)	(2,399)
Utilisation	(27)
Currency translation differences	1,911
Transfer to non-current assets held for sale (Note 23)	(68)
Closing balance as at 31 December 2016	**78,694**

22 - Cash and cash equivalents

As at 31 December 2016 and 2015, cash and cash equivalents is detailed as follows:

	2016	2015
Term deposits	11,278	69,085
Bank deposits available on demand	139,117	67,635
Cash	73	94
Cash and cash equivalent in the statement of financial position	**150,468**	**136,814**
Restricted cash	**538**	**4,177**
Bank overdrafts (Note 27)	**(280)**	**-**
Cash and cash equivalents in the cash flow statement	**150,726**	**140,991**

The amount of cash presented by the Group primarily arises from the cash of “TAP S.A.”, in the amount of Euro 75.322 thousand (2015: Euro 134.822 thousand) and of TAP SGPS in the amount of Euro 70.197 thousand (2015: Euro 157 thousand).

The bank deposits in Angola at 31 December 2016, in the amount of Euro 35,903 thousand (31 December 2015: Euro 27,691 thousand), are currently experiencing difficulties in repatriating the funds. In this regard, a current credit line was negotiated with a financial institution, limited to Dollar 20 million, which provides the Group with the amounts withheld in Angola. The bank deposits stand as collateral on the referred loan obtained. Additionally, the aforementioned cash will also be used to pay the local expenses of the air transport operation.

Surplus liquidity is normally invested in short term financial investments, earning interest at normal market rates.

Restricted cash

Despite the TAP Group attempts on the referred funds repatriation during 2015 TAP Group verified the existence of new data and unfavourable indicators to the repatriation of funds held in Venezuela, such as:

- More than one year has passed without any transfer of funds being authorised by the Venezuelan authorities despite the several payment promises given by different political representatives of that country to TAP Group;
- The sharp deterioration of Venezuela economic environment and consequently significant increase of its country-risk;
- The unsuccessful negotiation from IATA and from several Governments of the aviation companies that operate in Venezuela.
- The pressure perpetrated, fundamentally the second semester of 2015 onwards, by several local suppliers in order to: (i) demand the use of the SIMADI exchange rate for the payment of invoices denominated in US dollars; (ii) increase the price of invoices denominated in Venezuelan bolivars to a rate equivalent to the use of such exchange rate and (iii) charge, in dollars, invoices that traditionally were paid in Venezuelan bolivars, restricting significantly the TAP Group ability to spend locally the funds retained at the exchange rate correspondent to the one applied at the time of sale.

In this context, accompanying its peers, the Board of Directors understands that the best estimate for the exchange rate of restricted cash in Venezuela is SIMADI rate, which represented the recognition of a negative exchange variation (198,7 VEF/USD) in the amount of Euro 91 million in 2015 (Note 54).

During 2016, the continued deterioration of the country's economic situation led to a significant depreciation of the SIMADI rate (673.76 VEF/USD as of 31 December 2016). Consequently, at this date, it is the Board of Directors' understanding that the SIMADI rate is the best estimate for the exchange rate of Venezuelan restricted cash, which represented the recognition of a negative exchange rate variation in the approximate amount of Euro 2.6 million in the period ended 31 December 2016.

23 – Non-current assets and liabilities held for sale and discontinued operations

Following the decision to divest 51% of the capital held in the subsidiary L.F.P. - Lojas Francas de Portugal, SA, TAP Group carried out: (i) the reclassification of its assets and liabilities, in the consolidated statement of financial position, which are classified as non-current assets and liabilities held for sale and (ii) the restatement of the amounts recorded in the consolidated income statement for the year ended 31 December 2015, considering its classification as a discontinued operation.

It should also be noted that the transaction is pending approval by the Competition Authority, and it is estimated that the outcome will occur during the first half of 2017.

✈ Statement of financial position

Assets and liabilities from the referred subsidiary classified as held for sale as of 31 December 2016 are detailed as follows:

Amounts stated in thousand euros	Non-current assets /liabilities held for sale
Non-current assets	
Tangible fixed assets	7,683
Intangible assets	46
Deferred tax assets	234
	7,963
Current assets	
Inventories	16,307
Trade receivables	849
State and other public entities	1,233
Other receivables	5,850
Deferred expenses	1,362
Cash and cash equivalents	2,791
	28,392
Total Assets	**36,355**
Current liabilities	
Suppliers	19,157
State and other public entities	1,050
Other payables	2,717
Deferred revenue	339
Total liabilities	**23,263**

It should be noted that in accordance with IFRS 5, the amounts referring to the consolidated statement of financial position as of 31 December 2015 have not been restated.

✈ Income statement

The income and expenses of LFP, presented as result from discontinued operations, for the years ended 31 December 2016 and 2015 are detailed as follows:

Amounts stated in thousand euros	2016	2015
Sales and services rendered	207,282	189,214
Cost of goods sold and materials consumed	(126,319)	(116,619)
External supplies and services	(63,930)	(53,963)
Employee costs	(10,610)	(9,448)
Impairment in inventory (losses/reversals)	(172)	(58)
Impairment in receivables (losses/reversals)	-	(17)
Provisions (increases/decreases)	-	8
Other operational income	8,109	3,662
Other operational costs	(423)	(259)
Earnings before interests, taxes, depreciation and amortisation	**13,937**	**12,520**
Depreciation and amortisation costs	(2,030)	(846)
Operating income/(loss) (earnings before interests and taxes)	**11,907**	**11,674**
Finance income	-	2
Finance costs	(14)	(5)
Net income/(loss) before income tax	**11,893**	**11,671**
Income tax for the year	(2,949)	(3,009)
Net income for the year of discontinued operations	**8,944**	**8,662**

It should be noted that this amendment, referring to the financial year 2015, generated the restatement of the comparative figures as detailed below:

Amounts stated in thousand euros	2015	Restatement	2015 Restated
Sales and services rendered	2,597,936	(189,214)	2,408,722
Operating government grants	594	-	594
Gains and losses in associates	1,067	-	1,067
Variation in production	(8,589)	-	(8,589)
Internally generated assets	608	-	608
Cost of goods sold and materials consumed	(243,790)	116,619	(127,171)
External supplies and services	(1,718,345)	53,963	(1,664,382)
Employee costs	(566,405)	9,448	(556,957)
Impairment in inventory (losses/reversals)	148	58	206
Impairment in receivables (losses/reversals)	(5,672)	17	(5,655)
Provisions (increases/decreases)	178	(8)	170
Fair value increases/decreases	(174)	-	(174)
Other operational income	68,083	(3,662)	64,421
Other operational costs	(77,216)	259	(76,957)
Earnings before interests, taxes, depreciation and amortisation	**48,423**	**(12,520)**	**35,903**
Non-recurring items	(91,394)	-	(91,394)
Earnings before interests, taxes, depreciation and amortisation	**(42,971)**	**(12,520)**	**(55,491)**
Depreciation and amortisation costs	(62,697)	846	(61,851)
Operating income/(loss) (earnings before interests and taxes)	**(105,668)**	**(11,674)**	**(117,342)**
Finance income	4,633	(2)	4,631
Finance costs	(67,909)	5	(67,904)
Net income/(loss) before income tax	**(168,944)**	**(11,671)**	**(180,615)**
Income tax for the year	17,167	3,009	20,176
Net income from continuing operations	**(151,777)**	**(8,662)**	**(160,439)**
Results from discontinued operations	**-**	**8,662**	**8,662**
Net income/(loss) for the year	**(151,777)**	**-**	**(151,777)**

✈ Statement of cash flows

The cash flows related to aforementioned subsidiary for the years ended 31 December, 2016 and 2015 were considered as an integral part of this statement and are detailed as follows:

Amounts stated in thousand euros	2016	2015
Net cash flows of the operating activities	18,438	8,533
Net cash flows of the investing activities	(6,026)	(3,412)
Net cash flows of the financing activities	(10,576)	(5,255)
Discontinued operations net cash flows	**1,836**	**(134)**

24 – Equity

The nominal share capital of the Group, in the amount of Euro 5,000 thousand is represented by 1,500,000 nominal shares of 10 euros each, and is fully underwritten and paid-up. Following the re-privatization process of TAP Group, on 12 November 2015, 915,000 nominal shares, representative of 61% of share capital of TAP SGPS, were transferred to Atlantic Gateway, and Parpública remains with 39% of share capital of TAP SGPS.

✈ Supplementary Capital Contributions

Following the Shareholders General Meeting resolution on 12 November 2015, the shareholder Atlantic Gateway proceeded to a cash entry, fully realised, in the amount of Euro 154,353 thousands of supplementary capital contributions, in two phases, one of Euro 15,000 thousand and another of Dollar 150,000 thousand. These supplementary capital contributions are non-remunerated, do not have a defined maturity date and may not be reimbursed before a period of 30 years. If any reimbursement occurs after such period the respective deliberation has to be approved by, at least, 76% of the General Meeting members with voting rights.

In 2016, and following the TAP Group reprivatisation process, following the Shareholders General Meeting resolution on 29 March 2016, the shareholder Atlantic Gateway made cash inflows in four instalments of Dollar 19,188 thousand, fully paid-up, in the total amount of Dollar 76,750 thousand (Euro 69,740 thousand) , which characteristics are similar to the capital contributions that occurred in 2015, described above.

Additionally, in accordance with current legislation, supplementary capital contributions may only be reimbursed to shareholders if the total equity maintain greater than the sum of the share capital and the legal reserve.

✈ Legal reserves

The legal reserve was constituted in accordance with article 295 of the Commercial Companies Code, which establishes that, at least, 5% of annual net profit must be transferred to legal reserves until it reaches 20% of the company share capital. This reserve cannot be distributed, except in the case of the company's liquidation, but can be incorporated into the share capital or used to absorb losses after all other reserves have been depleted.

As at 31 December 2016 and 2015, the legal reserve was fully constituted in accordance with the commercial legislation in force.

✈ Foreign currency translation reserves

Foreign currency translation reserves resulting from the conversion of operating units denominated in foreign currency are recorded in equity, under this caption:

	2016			
	Opening balance	Increases	Decreases	Closing balance
TAP M&E Brasil and Aeropar:				
Currency translation of financial statements and goodwill	117,137	-	(50,815)	66,322
Extension of the net investment in TAP M&E Brasil	(187,543)	84,352	-	(103,191)
	(70,406)	**84,352**	**(50,815)**	**(36,869)**
			33,537	

	2015			
	Opening balance	Increases	Decreases	Closing balance
TAP M&E Brasil and Aeropar:				
Currency translation of financial statements and goodwill	71,028	46,109	-	117,137
Extension of the net investment in TAP M&E Brasil	(90,531)	-	(97,012)	(187,543)
	(19,503)	**46,109**	**(97,012)**	**(70,406)**
			(50,903)	

The decrease of Euro 50,815 thousand relates to the Group's appropriation of exchange differences resulting from the conversion of the financial statements of the companies operating in Brazil, in the unfavourable amount of Euro 73,084 thousand, and of the corresponding goodwill, in the favourable amount of Euro 22,269 thousand of (Note 7).

The increase of Euro 84,352 thousand in 2016 relates to the positive currency conversion differences arising from the medium and long-term loans granted to TAP M&E Brasil, whose settlement is unlikely to occur in the foreseeable future, and is, in substance, an extension of the group's net investment in this foreign operation.

The difference between the net reduction of the foreign currency translation reserves balance, amounting to Euro 33,537 thousand, and the amount recorded in the consolidated statement of comprehensive income in the amount of Euro 32,569 thousand, results from the amounts assigned to non-controlling interests.

✈ Hedge reserves

The negative amount of Euro 461 thousand (2015: negative amount of Euro 752 thousand) presented under the caption "Hedge reserves" corresponds to the fair value of the financial instruments classified as hedging accounting of the subsidiary TAP, S.A. recorded in accordance with the policy described in Note 2.12., net of tax, in the amount of Euro 175 thousand (2015: Euro 286 thousand) (Note 15).

As at 31 December 2016 and 2015, the derivative financial instruments fair value is detailed as follows:

	2016	2015
Interest rate swaps (Notes 31 and 58)	(636)	(1,038)
	(636)	**(1,038)**

The interest rate and jet fuel derivative financial instruments in portfolio, classified as hedging instruments presented the following evolution, during the financial years ended on 31 December 2016 and 2015:

	Liabilities	
	Current	Non-current
Fair value as at 1 January 2015	**(49,166)**	**(1,492)**
Acquisitions during the year - payment/(revenue)	35,241	-
Payment/(revenue) of swaps during the year	52,272	549
Revenue/(payment) of swaps retained through profit or loss	(87,513)	(549)
Increase/(decrease) of fair value reflected in equity	49,166	454
Fair value as at 31 December 2015	**-**	**(1,038)**
Acquisitions during the year - payment/(revenue)	-	-
Payment/(revenue) of swaps during the year	-	469
Revenue/(payment) of swaps retained through profit or loss	-	(469)
Increase/(decrease) of fair value reflected in equity	-	402
Fair value as at 31 December 2016	**-**	**(636)**

As at 31 December 2016 and 2015, the Group had no derivative financial instruments on jet fuel.

✈ Retained earnings

The caption "Retained earnings" corresponds to the net losses of previous years, as deliberated at the General Meetings. The impact that resulted from the first-time adoption of the International Financial Reporting Standards (IFRS) was also recorded under this caption, as well as gains or losses from the remeasurements of post-employment benefits, net of tax.

✈ **Results per share**

Considering that the convertible financial instruments on the shares of TAP SGPS, namely the convertible bonds, became effective with the approval of ANAC on 23 December 2016, the impact of the dilution of the result per share was considered to be fully immaterial (see detail in Note 1).

	2016	2015
Net income from continuing activities	(31,957)	(160,439)
Earnings/(losses) attributable to TAP SGPS shareholders	(27,731)	(156,042)
Weighted average number of shares	1,500,000	1,500,000
Basic and diluted earnings/(losses) per share from continuing activities (value in euro)	(21)	(107)
Basic and diluted earnings/(losses) per share from discontinued operations (value in euro)	3	3
Basic earnings/(losses) per share (value in euro)	(18)	(104)
Diluted earnings/(losses) per share (value in euro)	(18)	(104)

25 - Non-controlling interests

The non-controlling interests recorded in the statement of financial position are detailed as follows:

	%	2016	2015
Non-controlling interests of equity			
TAP M&E Brasil	1.36%	(5,336)	(3,785)
Cateringpor	49%	3,290	3,210
LFP	49%	5,521	5,382
		3,475	**4,807**

26 - Provisions

During 2016 and 2015, changes in provisions were as follows:

	2016						
	Opening balance	Increases	Reversal of unused amounts	Exchange rate variation	Other movements	Transfer to non-current liablities held for sale (Note 23)	Closing balance
Provisions							
Provision for legal claims (Note 45)	20,503	2,816	(3,284)	2,358	850	-	**23,243**
Provision for financial investments (Note 37)	3,063	-	(1,743)	-	(43)	-	**1,277**
Other provisions (Note 45)	2,560	-	(974)	297	38	-	**1,921**
	26,126	**2,816**	**(6,001)**	**2,655**	**845**	**-**	**26,441**

	2015						
	Opening balance	Increases	Reversed unused amounts	Exchange rate variation	Other movements	Reversed unused amounts from discontinued operations (Note 23)	Closing balance
Provisions							
Provision for legal claims (Note 45)	23,094	5,124	(5,494)	(3,174)	953	-	**20,503**
Provision for financial investments (Note 37)	4,059	-	(1,067)	-	71	-	**3,063**
Other provisions (Note 45)	2,570	253	(53)	(289)	87	(8)	**2,560**
	29,723	**5,377**	**(6,614)**	**(3,463)**	**1,111**	**(8)**	**26,126**

In 2016 and 2015, resulted gains of Euro 1.442 thousand and Euro 170 thousand, respectively, recorded under the caption "Provisions" (Note 45).

✈ Provision for legal claims

Provisions for legal claims are recognised in accordance with the Group's and its legal advisors risk assessments, based on historical success rates by type of legal action and probability of unfavourable outcomes for the Group. As at 31 December 2016, the existent provision, in the amount of Euro 23,243 thousand, aims to cover the risk of several lawsuits filed against the Group, in Portugal and foreign countries.

The detail of the provision for legal claims is as follows:

	2016	2015
Group (without the subsidiary TAP M&E Brasil)	11,188	11,121
Subsidiary TAP M&E Brasil	12,055	9,382
	23,243	**20,503**

As at 31 December 2016, the subsidiary TAP M&E Brasil faced about 1,847 labour claims (1,900 claims as at 31 December 2015). The subsidiary is a joint debtor of the labour liabilities related to the migration of employees from VARIG to TAP M&E Brasil in 2001 and 2002. Labour claims have been filed by former employees of VARIG against the subsidiary and against "TAP S.A." due to the dismissal of VARIG employees following the judicial auction sale of the production unit of VARIG, held in July 2006.

These labour claims can be divided into 4 categories: (i) union claims; (ii) claims filed by pilots; (iii) claims filed by former employees of VARIG against it and the Group, demanding the succession of the employment status and (iv) claims filed by service providers requesting the acknowledgement of the Group's liability for any recognised labour debts.

✈ Provision for financial investments

In 2016, the Group appropriated gains from the associate SPdH in the amount of Euro 1,743 thousand, which were recorded under the caption of "Gains and losses in associates" (Note 37). Moreover, the caption "Other movements", in the amount of Euro 43 thousand, corresponds to the appropriation of the losses arising from the remeasurement of post-employment benefits of SPdH, which were recorded in the Group's retained earnings.

In 17 March 2009, a consortium of three banks (BIG, Banif and Banco Invest) transferred the participation in SPdH (50.1%) to "TAP S.A." for Euro 31.6 million. On the same date and during the period in which the concentration process was pending at the Competition Authority, "TAP S.A." transferred the exercise of its voting and supervision rights, as majority shareholder of SPdH, to an independent entity of the Group.

On 19 November 2009, the Competition Authority following an in-depth investigation process adopted a decision of prohibition relative to the concentration operation, which consisted in the acquisition of the exclusive control of SPdH, by “TAP S.A.”, through the acquisition of a 50.1% stake of the share capital of SPdH.

The Competition Authority thus imposed the forced separation of SPdH through the Group’s disposal of its shares representing at least 50.1% of the share capital of SPdH. Until the sale, the regulator imposed that SPdH should be administered by a trustee, acting on behalf of the Competition Authority, and managing SPdH independently from the Group.

On 18 June 2012, a purchase and sale agreement was concluded between “TAP S.A.”, “TAP SGPS” and Portugália and between SPdH and Urbanos Grupo, SGPS, S.A. for the acquisition of 50.1% of the share capital of SPdH, which became effective from 20 July 2012 onwards, the date of the Competition Authority's deliberation regarding the decision of non-opposition to the aforesaid operation. In the meantime, on 17 October 2012, Pasogal SGPS, S.A. succeeded Urbanos Grupo, SGPS, S.A. in all rights and obligations that resulted from the agreement referred above and the shareholders' agreement.

SPdH operating licenses to provide handling services to third parties, at Lisbon and Oporto airports, in categories 3 (baggage handling), 4 (cargo and mail handling) and 5 (runway operations handling) of reserved access expired on 31 December 2011.

Portuguese Civil Aviation Institute ("INAC") had still not completed the international public tenders for issue of new licenses, and consequent selection of the second service provider in these reserved access categories for Lisbon and Oporto airports, in which SPdH was an opponent. Decree-Law nº 19/2012, of 27 January, has been published in the meantime.

This Decree-Law now enables INAC to extend, on an exceptional basis, the reserved access licenses to the ground handling service provider in the aforesaid reserved categories at Lisbon and Oporto airports, held by SPdH as at 31 December 2011, until the time when the ground handling service providers begin their activity, after being selected under the public tenders in progress.

Based on evolution of handling market in Portugal, it was announced the Order nº 14.886-A/2013, of 14 November, of the State Secretary for Infrastructure, Transport and Communications. These developments, consistent with the rationale behind the legislative proposals in discussion at the European Union institutions, highlighted the need to introduce a higher level of competition in handling services in order to reduce the costs of airline companies and, therefore, the prices charged to passengers.

The referred Order allowed the increase of the number of handling services providers, from two to three, in the categories 3, 4 and 5 at Lisbon, Oporto and Faro airports, subject to some conditions compliance related to the annual traffic and load volume.

INAC considered that fundamental assumptions that were on the basis for the international public tenders for Lisboa, Oporto and Faro have changed. Following this, INAC decided on the tenders cancellation and consequent revocation of the decision to hire, based on paragraph d) of number 1 of Article 79 and on number 1 of Article 80 of Public Procurement Law ("Código dos Contratos Públicos").

Following the above mentioned facts, Decree-Law nº 57/2014, of 11 April, was published, which amended article 4 of Decree-Law nº 19/2012, of 27 January. The article now states that the current licenses granting access to the activity of ground handling services in Lisbon, Oporto and Faro airports can be extended until 31 May 2015 or until the date on which the ground handling service providers, to be selected, begin their activity in the mentioned categories and airport infrastructures accordingly to article 27 of Decree-Law nº 27599, of 23 July, whichever is earlier.

In September 2014, Portuguese Civil Aviation Authority (ANAC), former INAC, initiated 9 public tenders to grant access licences to the activity of ground handling services in luggage, ground and cargo categories for Lisbon, Oporto and Faro airports. Only one licence is attributable in seven of the nine tenders, considering that in Lisbon, for luggage and ground, are attributable 2 licenses.

In 21 May 2015, ANAC issued a new access licence that extends the validity of the activity license for Lisbon, Oporto, Funchal and Porto Santo, initially issued with effects on 1 January 2005.

The tenders are still running on this date, except for services category 3, from Oporto Airport, whose access license was granted to SPdH on 11 November 2016 and with a validity period of 7 years.

The situation of SPdH with regard to the licensing of its activity in 2016 is as follows:

- As regards the categories of restricted access services (3, 4 and 5 for Lisbon Airport and 4 and 5 for Oporto Airport), the extensions to the corresponding activity access licenses, which had been issued on 1 January 2005, are in force until the selection of ground handling services providers in the scope of the International Public Tenders Restricted by Prior Qualification and the respective start of the activity.

- For unrestricted service categories the licenses remain valid until the end of the respective public utilisation licenses. Thus, licenses for the use of the public airport domain applicable to Lisbon and Oporto for the unrestricted service categories are valid until 31 December 2022.

- Regarding the access license applicable to the airports of Madeira and Porto Santo, whose extension ended on 31 December 2016, SPdH requested the extension for an additional period of 7 years, which was formalised on 23 September 2016.

It should be noted that if SPdH is not selected as the handling service provider in future international public tenders launched by ANAC, Pasogal SGPS, S.A. will have the right to dissolve the aforesaid purchase and sale agreement.

As at 31 December 2016 and 2015, the financial information relative to the associate SPdH is as follows:

	2016				
	Total assets	Total equity	Total liabilities	Sales and services rendered	Net income for the year
SPdH	**30,363**	**7,672**	**22,691**	**113,935**	**6,107**

	2015				
	Total assets	Total equity	Total liabilities	Sales and services rendered	Net income for the year
SPdH	**22,551**	**1,565**	**20,986**	**108,048**	**1,284**

✈ Other provisions

This caption is detailed as follows:

	2016	2015
Subsidiary TAP M&E Brasil:		
Provision for tax contingencies	864	693
Provision for civil contingencies	573	422
Remaining subsidiaries:		
Other provisions	484	1,445
	1,921	**2,560**

Provision for tax and civil contingencies

The subsidiary TAP M&E Brasil is currently involved in tax proceedings, both in the administrative and judicial sphere, which, when applicable, are guaranteed by judicial deposits and/or pledging of assets.

In 2009 the subsidiary TAP M&E Brasil joined the Tax Recovery Programme, called REFIS, through which it defined an instalment plan of all its federal contingencies with success probability classified as remote, compensating part of the interest and contingency fines with deferred rent tax and social security contributions, over the total tax losses carried forward and negative social security contribution base ("CSLL"), having reduced its debt by Euro 49,448 thousand.

On 9 July 2014, Provisional Measure nº 651/2014 (MP 651, converted into Law 13.043/14) was published which, among other issues, allowed the taxpayer to pay tax debts in advance, once the instalment plan was agreed, with the use of own credits from tax losses carried forward and negative calculation base of CSLL.

Considering this, TAP M&E Brasil, following the legal recommendation of the respective lawyer on the legal conditions required to benefit from the measures regulated by article 33 of the Provisional Measure, decided that criteria were met. Consequently, the Company paid 30% of the debt in the amount of Real 71,234 thousand and settled the rest with the tax credits arising from tax losses and from a negative social security contribution base in the amount of Real 166,214 thousand (Euro 51,594 thousand). This gain was recognised, in 2014, in the caption of "Other operational income", taking into consideration that this gain resulted essentially from social security contributions that were recorded in operating costs.

In addition, due to the accounting criteria adopted, the subsidiary requested a legal opinion on the tax treatment relative to the effects arising from the settlement of REFIS based on the tax credits arising from tax losses and from a negative social security contribution base. It is thus observed that it is a change in the form of use of an existing right, and thus no new right was created, regardless of its accounting classification. Considering this, the operating gain resulting from the compensation of the subdivision was not subject to corporate income tax, social integration programme ("PIS") and contribution to the financing of social security ("COFINS").

The movement in the provision for tax and civil contingencies was as follows:

Balance as at 1 January 2015	**1,099**
Provision increase/decrease	252
Reversal by revised estimate	(34)
Currency translation differences	(289)
Other movements	87
Balance as at 31 December 2015	**1,115**
Reversal by revised estimate	(13)
Currency translation differences	297
Other movements	38
Balance as at 31 December 2016	**1,437**

27 - Borrowings

Borrowings are detailed as follows:

	2016		2015	
	Current	Non-Current	Current	Non-Current
Bank loans	196,937	445,878	108,133	521,803
Bond loan	-	126,003	-	-
Leasing liabilities	131,057	94,960	90,664	221,567
Bank overdrafts (Note 22)	280	-	-	-
	328,274	**666,841**	**198,797**	**743,370**

✈ Net debt

As at 31 December 2016 and 2015, net debt is detailed as follows:

	2016	2015
Borrowings		
Non-current	666,841	743,370
Current	328,274	198,797
	995,115	**942,167**
Cash and cash equivalents (Note 22)		
Cash	73	94
Bank deposits available on demand	139,117	67,635
Term deposits	11,278	69,085
	150,468	**136,814**
Net debt	**844,647**	**805,353**

✈ Bank loans

As at 31 December 2016 and 2015, bank loans are detailed as follows:

	2016	2015	Reference Rate
Non-current			
TAP SGPS			
BCP Bank Loan	1,827	1,827	Euribor 3m
TAP S.A.			
Montepio Geral Bank Loan	113,179	39,490	Euribor 3 m
CGD Bank Loan	96,834	121,462	Euribor 6 m
BIC Bank Loan	79,923	79,951	Euribor 3 m
BCP Bank Loan	49,416	74,009	Euribor 3 m
Novo Banco Bank Loan	41,946	66,738	Euribor 3 m
PK Bank Loan	24,689	-	Euribor 3 m
Deutsche Bank Loan	22,179	77,551	Taxa fixa
Banco Popular Bank Loan	15,885	15,859	Euribor 6 m
BPI Bank Loan	-	24,942	Euribor 6 m
Santander Bank Loan	-	19,974	Euribor 12 m
	445,878	**521,803**	
Current			
TAP SGPS			
BCP Bank Loan	14	14	Euribor 3m
TAP S.A.			
Deutsche Bank Loan	56,794	73,280	Taxa fixa
BCP Bank Loan	25,222	124	Euribor 3 m
BPI Bank Loan	25,214	17	Euribor 6 m
CGD Bank Loan	25,180	209	Euribor 6 m
Novo Banco Bank Loan	25,158	371	Euribor 3 m
Santander Bank Loan	19,983	-	Euribor 12 m
BIC credit line	18,976	18,373	Libor 6m
Montepio Geral Bank Loan	268	133	Euribor 3 m
PK Bank Loan	80	-	Euribor 3 m
Banco Popular Bank Loan	48	49	Euribor 6 m
Anticipation of Brazil's revenues - with resourse	-	13,663	Taxa fixa
LFP			
BPI Bank Loan	-	1,900	Euribor 3m
	196,937	**108,133**	
Bank debt	**642,815**	**629,936**	

In the context of re-privatization process, accordingly to the Direct Sale Agreement complemented with the Debt Service Agreement on Economic and Financial Stability of TAP Group, referred in Note 1, on 12 November 2015 TAP SA bank debt was restructured, being the main changes related to the maturity of the loans. A new bank debt restructuration is currently in progress (Note 1).

The remunerated bank loans, by maturity and type of interest rate, as at 31 December 2016 and 2015, is detailed as follows:

Maturity	2016	2015
Up to 1 year	196,937	108,133
1 to 2 years	7,301	173,919
2 to 3 years	89,753	7,354
3 to 4 years	98,170	83,007
4 to 5 years	93,577	84,749
Over 5 years	157,077	172,774
	642,815	**629,936**

Type of interest rate	2016	2015
Variable rate		
Up to 1 year	140,143	21,190
1 to 2 years	-	118,659
2 to 3 years	82,359	-
Over 3 years	341,340	325,593
	563,842	**465,442**
Fixed rate		
Up to 1 year	56,794	86,943
1 to 2 years	7,301	55,260
2 to 3 years	7,394	7,354
Over 3 years	7,484	14,937
	78,973	**164,494**
	642,815	**629,936**

The detail of the bank loans, by functional currency, as at 31 December 2016 and 2015 is as follows:

	Values in foreign currency	Values in Euros	Values in foreign currency	Values in Euros
Loans in Euros (EUR)	623,839	623,839	597,900	597,900
Loans in American Dollars (USD)	20,003	18,976	20,000	18,373
Loans in Brazilian Real (BRL)	-	-	58,911	13,663
		642,815		**629,936**

The chapter related to interest rate risk (Note 3) presents the bank loans liabilities and estimated interest expense until the loans maturity.

✈ Bond Loan

By resolution of TAP SGPS General Meeting on 8 March 2016, previously authorised by ANAC, was approved the issuance by TAP SGPS of a convertible bond, into TAP SGPS shares in the amount of Euro 120 million. The aforementioned issue is composed by two series: the first (series A), in the amount of Euro 90 million, subscribed by Azul S.A. and the second series (series B), in the amount of Euro 30 million, subscribed by

Parpública (Note 1). As of 31 December 2016, to the principal amount of Euro 120 million, adds interest payable in the amount of Euro 6,003 thousand.

✈ Financial leases

The Group records the assets acquired under financial leases as tangible fixed assets. As at 31 December 2016 and 2015, the Group had commitments arising from financial leases liabilities as described in Note 5, with the corresponding principal being included in the statement of financial position under the caption "Borrowings", as follows:

	2016	2015
Financial leases debt		
Basic equipment	225,233	312,148
Other tangible fixed assets	784	83
	226,017	**312,231**
Future payments of principal		
Up to 1 year	131,057	90,664
1 to 5 years	94,949	221,567
Over 5 years	11	-
	226,017	**312,231**

The financial leases liabilities, by maturity and type of interest rate, as at 31 December 2016 and 2015, are detailed as follows:

Maturity	**2016**	**2015**
Up to 1 year	131,057	90,664
1 to 2 years	52,364	127,445
2 to 3 years	31,450	52,046
3 to 4 years	10,887	31,447
4 to 5 years	122	10,629
Over 5 years	137	-
	226,017	**312,231**

Type of interest rate	**2016**	**2015**
Variable rate		
Up to in 1 year	34,343	47,873
1 to 2 years	27,213	34,047
2 to 3 years	6,019	27,030
Over 3 years	379	6,163
	67,954	**115,113**
Fixed rate		
Up to in 1 year	96,714	42,791
1 to 2 years	25,151	93,398
2 to 3 years	25,431	25,016
Over 3 years	10,767	35,913
	158,063	**197,118**
	226,017	**312,231**

Financial leases, by functional currency, are detailed as follows:

	2016	2015
Financial leases in EUR	137,701	205,773
Financial leases in USD (Note 3)	88,316	106,456
Financial leases in BRL (Note 3)	-	2
	226,017	**312,231**

The chapter related to interest rate risk (Note 3) presents the financial leases liabilities and estimated interest expense until the leases maturity.

Some borrowings have real guarantees, namely financial leases, loan from BIC and Montepio and the convertible bond.

✈ Operating leases

As referred to in Note 2.25., these liabilities are not recorded in the Group's consolidated statement of financial position. Group's operating leases contracts have different periods which may reach up to 7 years, which may be extended through the explicit consent of the contracting parties.

As at 31 December 2016, forty four aircrafts (Note 5) and four engines were under operating lease contracts.

As at 31 December 2016 and 2015, the financial commitments assumed by the subsidiary TAP S.A. and Portugália relative to operating lease contracts for aircraft and engines reached the total of Euro 435,539 thousand (Dollar 470,382 thousand). As of 31 December 2015, these commitments were only related to TAP SA amounting some Euro 342,014 thousand (Dollar 366,639 thousand) (Note 60).

The payment schedule for the operating lease agreements are detailed as follows:

	2016	2015
Up to 1 year	120,906	85,276
1 to 2 years	107,801	76,960
2 to 3 years	84,563	67,240
3 to 4 years	54,311	52,476
Over 4 years	67,958	60,062
	435,539	**342,014**

These contracts require security deposits which, as at 31 December 2016 and 2015, reached a total of Euro 29,750 thousand and Euro 12,954 thousand, respectively (Note 18). These deposits shall be returned to the Group when each of these aircraft is handed back to its lessor.

✈ **Financial covenants**

The financial covenants in the lease and loan contracts are the usual ones in operations of this nature, including compulsory provisions such as the maintenance of the airline operator activity, commitments to periodically disclose the available financial information, and, in the specific case of financial leases, operating duties relative to registrations at official entities, information relative to leased aircraft, strict compliance with all the regulations, and procedures defined by the authorities, amongst others.

Additionally, in the context of the bank debt restructure referred above and the bond issuance, some commitments were assumed regarding the follow up of the Group's financial performance, through the analysis and accomplishment of certain ratios related to equity, EBITDAR, unsecured financial net debt and minimum amount of unrestricted cash and cash equivalents. These ratios have as main objective to follow up the Group's financial situation and its capability to repay the debt.

28 – Post-employment benefits obligations

The Group has responsibility for post-employment benefits payments to employees who have retired, due to their age, taken early retirement or are still active.

✈ **Retirement pension supplements and early retirement instalments – "TAP S.A."**

Pursuant to the current rules at "TAP S.A.", employees who joined the company before 31 May 1993 are entitled to receive the difference between the state retirement pension paid by the Social Security System, due to the age limit or invalidity, plus a minimum amount assured by "TAP S.A." This amount corresponds to a fixed percentage of part of the pensionable salary (base remuneration + annuities) at the time of retirement, for each year of work at the company, up to a maximum of 20 years, as follows:

- Flight deck crew (pilots and flight technicians) - 3.2% per year of service;
- Ground staff and cabin crew - 4% per year of service.

In addition, "TAP S.A." has undertaken to pay early retirement pensions, whose value is fixed so that the respective net value receivable in situations of early retirement ranges from 75% to 100% of the net value that the employees received when active on the date of early retirement.

In October 2008, the Labour Agreement with the Civil Aviation Pilots Union (SPAC) was amended, with the following main changes:

- <u>Pilots recruited before 31 May 2007</u>: the pension plan includes the seniority bonus guaranteed by the State (of 15% or 10%, according to the starting date of the contributory career) and the possibility of an additional bonus (up to 25% or 30%) as an option for the beneficiary upon retirement (this additional bonus of up to 25% will be paid by “TAP S.A.”);

- Pilots recruited as of 1 June 2007: the pension plan consists of a defined contribution scheme of 7.5% of the base remuneration effectively earned (14 times a year), of which 80% is paid by “TAP S.A.” This plan is guaranteed by contracts of participation in open pension funds managed by Banco Português de Investimento ("BPI"). The participation contracts and their management are optional to SPAC, as established in the collective regulations.

“TAP S.A.” has recorded all its liabilities related to past services for the payment of pension supplements and early retirement benefits relative to the defined benefit plan.

The quantification of the liabilities took into consideration that, under the terms of the collective regulations establishing the aforesaid pension plan, the total pension guaranteed by “TAP S.A.”, i.e., the social security pension and pension supplement will never exceed the base monthly remuneration, net of personal income tax (IRS) and social security payments during employment. This premise is not applicable, since it is not established in the collective regulations relative to flight deck crew, for whom this limit does not apply and the pensionable salary is made up of the base salary set out in the pay scale, plus monthly earnings in the financial year and seniority bonuses.

In order to cover the liabilities related to the defined benefit plan, “TAP S.A.” concluded a contract of participation in the VIVA open pension fund. As of 2011, the cost related to retirement pension supplements, constituted since 1998, is assumed by this participation. Annual expenditure on pensions is determined in accordance with the actuarial study, reviewed and adjusted annually according to the updating of salaries and the evolution of the participant group. Costs relative to retirement supplements constituted by December 1997, early retirement instalments and the portion of pilot retirement supplements, which exceeds the limit referred to in the preceding paragraph, are assumed directly by “TAP S.A.” and covered by a specific provision.

✈ **Pensions - TAP M&E Brasil**

From 1 January 2002 onwards, the subsidiary TAP M&E Brasil became one of the sponsors of the AERUS Social Security Institute (AERUS), by means of the supplementary retirement pension plan assured to its employees, in the form of defined contributions, named Benefit Scheme II - VEM.

In 2008, the subsidiary requested the transfer of the manager of the benefits fund of its employees from the entity AERUS. This process was initially refused by the holding company of the AERUS fund, which claimed that TAP M&E Brasil had debts that were not recognised in the transfer of liabilities related to post-employment benefits, since it was jointly liable for the pension fund deficits of other sponsors. TAP M&E Brasil questioned the legal validity of this debt and the competent entities declared there was no reason for opposing the transfer mentioned above, such that, on 15 June 2012, the transfer was successfully carried out to the Benefit Scheme of the Petrobrás Social Security Foundation (PETROS), and renamed the TAPMEPreve Plan.

In spite of being a "defined contribution" benefit plan, this scheme also offers invalidity and death benefits under the concept of "defined benefits", in addition to guaranteeing special benefits to a group of employees from VARIG who were integrated in the staff of the subsidiary when the operations of this company were demerged.

Therefore, only the defined benefit component referred to above is recorded under the caption "Post-employment benefits obligations".

✈ **Pensions – Portugália**

Portugália established a defined contribution scheme for flight deck crew on 1 January 2010. This scheme is managed by BPI, to which the subsidiary contributes 6% of the monthly wage effectively earned by the pilots, 14 times a year. Employees make social security payments of 1.5%, and can also make supplementary payments of 1% to 5%.

✈ **Pensions – UCS**

UCS is responsible, according to internal regulations, for granting, through a defined benefit scheme, retirement pension supplements for the part which exceeds those that are granted by Social Security. In order to cover this liability, the Company subscribed to the Horizonte Valorização Pension Fund. Annual expenditure on pensions, which includes contributions to the fund, is determined in accordance with the actuarial study, reviewed and adjusted annually according to the updating of salaries and the evolution of the participant group.

✈ **Seniority bonus - PNT - “TAP S.A.”**

The Company Agreement concluded between “TAP S.A.” and SPAC establishes that “TAP S.A.” undertakes to pay to pilots recruited before 31 May 2007, in addition to a pension scheme, a one-off retirement bonus to every pilot upon retirement due to old age, which is funded by the capital accumulated in a collective insurance policy constituted by “TAP S.A.” on behalf of the pilots. The main conditions of the collective retirement policy agreed with the insurance company, describing this Retirement Benefits Plan for Pilots, are as follows:

- Admission conditions: pilots who are still in active service;
- Normal retirement age: 65 years old;
- Guarantees: each participant is entitled, upon the retirement date, to an amount equal to 16 times the last declared monthly wage.

The Benefit Plan is funded through an insurance policy that is reinforced by contributions (premiums) paid by "TAP S.A." and by income obtained from investments made by the insurance company in an Autonomous Fund which supports this type of insurance.

In October 2008, the agreement between the Company and SPAC was amended, with the main changes being as follows:

- Pilots recruited before 31 May 2007: the one-off seniority bonus is maintained, but shall only be paid if, on the retirement date, the person is entitled to the full pension, with the possibility of increasing the capital for every additional year of service after the full pension age has been reached;

- Pilots recruited as of 1 June 2007: there is no entitlement to seniority bonus.

✈ **Health Care – "TAP S.A."**

"TAP S.A." ensures that both pre-retired and early-retired employees, below the age of 65, are provided with a health care plan providing access to medical care at reduced prices. In addition, "TAP S.A." provides its retired employees with access to UCS medical services, as a freely granted benefit, for which they pay a portion of the cost of each clinical service with the remainder being paid by "TAP S.A."

"TAP S.A." considers that although it provides its former employees with access to the health care services of UCS, this is not a liability but a freely granted benefit at any given time. Therefore the company assumes no accounting liability regarding the provision of health care services to current employees after they cease working for the company. As such, at the present time, the existing provision covers the total responsibility for medical treatment with former employees. The total responsibility was calculated based on an independent actuarial evaluation.

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Assumptions used in the evaluation of liabilities

The liabilities of the different companies of the Group were calculated through actuarial studies reported as at 31 December 2016 and 2015, prepared by independent entities, individually for each company, using the projected unit credit method and essentially based on the following financial and demographic assumptions:

	2016		2015	
	Portugal	Brazil	Portugal	Brazil
Mortality table	TV 88/90	AT2000	TV 88/90	AT2000
Invalidity table	EKV1980	Winklevoss	EKV1980	Winklevoss
Discount rate	2.00%	11.59%	2.50%	13.15%
Fund yield rate	2.00%	11.59%	2.50%	13.15%
Growth rate				
Wages	1.50%	6.56%	1.50%	6.56%
Pensions	1.00%	5.50%	1.00%	5.50%
Trend of medical costs	1.50%	--	1.50%	--

The net liabilities evolution for past services, as at 31 December 2016 and 2015 is detailed as follows:

	2016	2015
Liabilities for past services at the beginning of the year	**54,268**	**56,626**
Net interest	1,278	2,043
Cost of current services	3,860	3,622
Pensions fund contributions	(5,174)	(5,218)
Remeasurements	16,054	2,731
Exchange rate changes in the plans measured in a different currency	1,085	(1,635)
Benefits paid	(3,683)	(3,901)
Liabilities for past services at the end of the year	**67,688**	**54,268**

Liabilities for 2016 and 2015 are detailed as follows:

	2016								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Liabilities from past services									
- Active employees	359	-	2,313	-	67,777	-	9,545	122	80,116
- Early retirement	61	-	367	32	-	-	-	-	460
- Retired	9,959	35,424	-	2,908	-	16,133	68,680	-	133,104
Fair value of the funds	(16,280)	-	-	-	(49,145)	(14,806)	(65,639)	(653)	(146,523)
Deficit / (surplus)	**(5,901)**	**35,424**	**2,680**	**2,940**	**18,632**	**1,327**	**12,586**	**(531)**	**67,157**

	2015								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Liabilities from past services									
- Active employees	324	-	1,841	-	58,921	-	-	9	61,095
- Early retirement	83	-	456	45	-	-	51,319	-	51,903
- Retired	9,951	37,197	-	2,957	-	15,859	-	-	65,964
Fair value of the funds	(16,792)	-	-	-	(44,527)	(15,641)	(47,725)	(646)	(125,331)
Deficit / (surplus)	**(6,434)**	**37,197**	**2,297**	**3,002**	**14,394**	**218**	**3,594**	**(637)**	**53,631**

The surplus financing of the Horizonte Valorização Pension Fund of the subsidiary UCS, in the amount of Euro 531 thousand, is recorded under the caption "Other receivable" (2015: Euro 637 thousand) (Note 18).

The liabilities between 2012 and 2014 are detailed as follows:

2014	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Liabilities from past services									
- Active employees	646	-	1,782	-	51,203	-	-	37	53,668
- Early retirement	129	-	476	87	-	-	9,065	-	9,757
- Retired	10,536	39,836	-	3,116	-	15,767	58,475	-	127,730
Fair value of the funds	(16,954)	-	-	-	(39,595)	(15,549)	(62,394)	(620)	(135,112)
Deficit / (surplus)	**(5,643)**	**39,836**	**2,258**	**3,203**	**11,608**	**218**	**5,146**	**(583)**	**56,043**

2013	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Liabilities from past services									
- Active employees	1,739	-	1,062	-	39,334	-	-	5	42,140
- Early retirement	258	-	2,306	166	-	-	8,557	-	11,287
- Retired	9,765	38,569	-	2,948	-	16,180	51,903	-	119,365
Fair value of the funds	(16,443)	-	-	-	(35,218)	(14,948)	(58,585)	(587)	(125,781)
Deficit / (surplus)	**(4,681)**	**38,569**	**3,368**	**3,114**	**4,116**	**1,232**	**1,875**	**(582)**	**47,011**

2012	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Liabilities from past services									
- Active employees	2,214	-	419	-	35,747	-	-	7	38,387
- Early retirement	2,197	-	2,970	254	-	-	90,056	-	95,477
- Retired	9,442	39,994	-	2,739	-	13,958	153	-	66,286
Fair value of the funds	(15,943)	-	-	-	(32,106)	(13,131)	(67,937)	(554)	(129,671)
Deficit / (surplus)	**(2,090)**	**39,994**	**3,389**	**2,993**	**3,641**	**827**	**22,272**	**(547)**	**70,479**

According to the actuarial study carried out by an independent entity, the best estimate of contributions to the pension benefit plans, for the following financial year, is 6,679 thousand euros for the subsidiary "TAP S.A." and Euro 3,410 thousand for the subsidiary TAP M&E Brasil.

As at 31 December 2016 and 2015, the defined benefit plans of the Group in Portugal (excluding the Representation in England and Brazil) covered 2,232 and 2,270 active beneficiaries, respectively. The total number of retired former employees entitled to a supplementary retirement pension, as at 31 December 2016 and 2015, was 808 and 840 beneficiaries, respectively.

As at 31 December 2016, the average maturity of the liabilities related to the defined benefit plan for the VIVA open pension fund is 12 years (2015: 10.8 years), for the Seniority Bonus plan it is 12 years (2015: 13 years).

Sensitivity analysis

✈ Annual discount rate

An increase (decrease) of 0.25% in the annual discount rate of the defined benefit plans of the VIVA open pension fund, Seniority Bonus scheme and Horizonte Valorização Pension Fund, and an increase (decrease) of 1% in the annual discount rate of the TAPMEPrev - Brazil defined benefit plan, would correspond to the following impacts on the Group's liabilities as at 31 December 2016:

	Rate	VIVA Pensions *	Seniority Bonus	Horizonte Valorização Pension Fund
Annual discount rate of pensions	2.00%	48,483	67,777	122
0.25% increase in the discount rate	2.25%	47,420	65,275	119
0.25% decrease in the discount rate	1.75%	49,591	70,401	124

* Includes "Pensions VIVA", "Before 1997" and "Assets"

	Rate	Brazil
Annual discount rate of pensions	11.59%	78,225
1% increase in the discount rate	12.59%	71,349
1% decrease in the discount rate	10.59%	86,461

✈ Rate of growth of medical costs

If the growth rate of medical care costs increases or decreases by one percentage point, the respective impact on the Group's liabilities as at 31 December 2016 and 2015 is as follows:

	Rate	2016	2015
Annual growth rate of medical costs	1.50%	2,940	3,002
1% increase in the growth rate of medical costs	2.50%	3,192	3,262
1% decrease in the growth rate of medical costs	0.50%	2,718	2,773

Evolution of liabilities from past services

The movement of the liabilities from past services, reflected in the consolidated statement of financial position, as at 31 December 2016 and 2015, is as follows:

	2016								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Liabilities at the beginning of the year	10,358	37,197	2,297	3,002	58,921	15,859	51,319	9	178,962
Exchange rate variation	-	-	-	-	-	(1,779)	14,415	-	12,636
Values recorded through profit or loss for the year:									
Current services	31	-	-	-	3,734	-	95	14	3,874
Net interest	258	744	243	75	1,250	866	6,853	1	10,290
Remeasurements	522	1,166	140	(137)	4,329	1,757	10,157	98	18,032
Benefits paid	(790)	(3,683)	-	-	(457)	(570)	(4,614)	-	(10,114)
Responsibilities at the end of the year	**10,379**	**35,424**	**2,680**	**2,940**	**67,777**	**16,133**	**78,225**	**122**	**213,680**

	2015								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Liabilities at the beginning of the year	11,311	39,836	2,258	3,203	51,203	15,767	67,540	37	191,155
Exchange rate variation	-	-	-	-	-	-	(17,583)	-	(17,583)
Values recorded through profit or loss for the year:									
Current services	58	-	-	-	3,343	-	221	12	3,634
Net interest	283	996	57	80	1,369	92	7,076	1	9,954
Remeasurements	(733)	266	(18)	(281)	3,922	-	(1,996)	(41)	1,119
Benefits paid	(561)	(3,901)	-	-	(916)	-	(3,939)	-	(9,317)
Responsibilities at the end of the year	**10,358**	**37,197**	**2,297**	**3,002**	**58,921**	**15,859**	**51,319**	**9**	**178,962**

Evolution of funds allocated to pensions benefit schemes

In 2016 and 2015 the fund assets evolution was as follows:

	2016					
	VIVA Pensions	Seniority Bonus	England Representation	Brazil	UCS	Total
Opening balance	16,792	44,527	15,641	47,725	646	125,331
Exchange rate variation	-	-	(1,496)	13,047	-	11,551
Contributions in the year	-	4,200	-	974	-	5,174
Net interest	278	1,113	1,112	6,508	7	9,018
Remeasurements	-	(238)	119	1,999	-	1,880
Benefits paid	(790)	(457)	(570)	(4,614)	-	(6,431)
Closing balance	**16,280**	**49,145**	**14,806**	**65,639**	**653**	**146,523**

	2015					
	VIVA Pensions	Seniority Bonus	England Representation	Brazil	UCS	Total
Opening balance	16,954	39,595	15,549	62,394	620	135,112
Exchange rate variation	-	-	-	(15,948)	-	(15,948)
Contributions in the year	-	4,656	92	470	-	5,218
Net interest	399	990	-	6,521	26	7,936
Remeasurements	-	202	-	(1,773)	-	(1,571)
Benefits paid	(561)	(916)	-	(3,939)	-	(5,416)
Closing balance	**16,792**	**44,527**	**15,641**	**47,725**	**646**	**125,331**

The composition of the funds and its category as at 31 December 2016 and 2015 is as follows:

	2016						
	Fair Value Level	VIVA Pensions	Seniority Bonus	England Representation	Brazil	UCS	Total
Shares	1	4,995	-	9,377	8,533	163	23,068
Bonds	1	4,964	47,897	4,019	57,106	457	114,443
Public debt	1	4,859	-	-	-	-	4,859
Real estate	2	547	383	-	-	33	963
Liquidity	1	915	865	-	-	-	1,780
Other current investments	1	-	-	1,410	-	-	1,410
		16,280	**49,145**	**14,806**	**65,639**	**653**	**146,523**

	2015						
	Fair Value Level	VIVA Pensions	Seniority Bonus	England Representation	Brazil	UCS	Total
Shares	1	4,921	-	9,906	6,204	169	21,200
Bonds	1	4,861	43,659	4,245	41,521	435	94,721
Public debt	1	4,965	-	-	-	-	4,965
Real estate	2	586	347	-	-	25	958
Liquidity	1	1,459	521	-	-	17	1,997
Other current investments	1	-	-	1,490	-	-	1,490
		16,792	**44,527**	**15,641**	**47,725**	**646**	**125,331**

Expenses related to pensions and other post-employment benefits

The expenses relative to pensions and other post-employment benefits are detailed as follows:

	2016								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Current Services	31	-	-	-	3,734	-	95	14	3,874
Net interest	(18)	744	243	75	138	(246)	342	(6)	1,272
	13	**744**	**243**	**75**	**3,872**	**(246)**	**437**	**8**	**5,146**

	2015								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority Bonus	England Representation	Brazil	UCS	Total
Current Services	58	-	-	-	3,343	-	221	12	3,634
Net interest	(116)	996	57	80	379	92	555	(25)	2,018
	(58)	**996**	**57**	**80**	**3,722**	**92**	**776**	**(13)**	**5,652**

As previously mentioned, the pilots of TAP S.A., admitted after 1 June 2007, and the pilots of Portugália, benefit from a defined contribution plan. During 2016, a cost was recognised in the heading “Employee costs - expenses related to post-employment benefits obligation" in the amount of Euro 1,723 thousand (2015: Euro 1,739 thousand), relative to the contributions made during the year in favour of its employees.

The expenses relative to pensions and other post-employment benefits for 2016 and 2015 are recorded under the caption "Employee costs" (Note 42).

Remeasurement gains/losses

The remeasurement gains/losses related to post-employment benefit plans are detailed as follows:

	2016								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority bonus	England Representation	Brazil	UCS	Total
Remeasurements									
Return of assets, excluding amounts included in net income	-	-	-	-	238	(119)	(1,999)	-	(1,880)
	-	**-**	**-**	**-**	**238**	(119)	(1,999)	-	**(1,880)**
(Gains)/losses due to changes in demographic assumptions	-	-	-	-	-	-	59	-	59
(Gains)/losses due to changes in financial assumptions	478	1,403	160	-	5,135	-	9,375	-	16,551
(Gains)/losses due to experience	44	(237)	(20)	(137)	(806)	1,757	723	98	1,422
	522	**1,166**	**140**	**(137)**	**4,329**	**1,757**	**10,157**	**98**	**18,032**
Total remeasurements	**522**	**1,166**	**140**	**(137)**	**4,567**	**1,638**	**8,158**	**98**	**16,152**

	2015								
	VIVA Pensions	Before 1997	Assets	Medical acts	Seniority bonus	England Representation	Brazil	UCS	Total
Remeasurements									
Return of assets, excluding amounts included in net income	-	-	-	-	(202)	-	1,773	-	1,571
	-	**-**	**-**	**-**	**(202)**	-	1,773	-	**1,571**
(Gains)/losses due to changes in demographic assumptions	-	-	-	-	(211)	-	141	-	(70)
(Gains)/losses due to changes in financial assumptions	-	-	-	-	-	-	(4,454)	-	(4,454)
(Gains)/losses due to experience	(733)	266	(18)	(281)	4,133	-	2,317	(41)	5,643
	(733)	**266**	**(18)**	**(281)**	**3,922**	**-**	**(1,996)**	**(41)**	**1,119**
Total remeasurements	**(733)**	**266**	**(18)**	**(281)**	**3,720**	**-**	**(223)**	**(41)**	**2,690**

The remeasurement gains/losses were recognised directly in the Group's comprehensive income. The difference to the amount recognised in the consolidated statement of comprehensive income relates to the remeasurements of the associated company SPdH, consolidated by the equity method (Note 26), in the amount of Euro 43 thousand (2015: Euro 70 thousand).

29 - Advances from customers

As at 31 December 2016 and 2015, the carrying amount of the caption "Advances from customers" is detailed as follows:

	2016	2015
Ministère de la Défense	308	308
Angola Airlines - TAAG	237	230
Travel agencies	147	89
Misc. passengers	64	81
Other	647	551
	1,403	**1,259**

30 - Suppliers

As at 31 December 2016 and 2015, the carrying amount of the heading "Suppliers" is detailed as follows:

	2016	2015
Suppliers - current account	120,085	153,391
Suppliers - invoices pending	31,598	14,452
	151,683	**167,843**

As at 31 December 2016 and 2015, this caption is detailed as follows:

	2016	2015
ANA - Aeroportos de Portugal, S.A.	27,888	49,865
TAP ME Brazil Suppliers	26,619	20,206
Petrogal	8,080	7,867
Eurocontrol - EU	7,935	7,908
Petrobras Distribution	3,428	1,676
CFM international, SA	2,756	769
Related parties (note 56)	1,916	6,862
Others	73,061	72,690
	151,683	**167,843**

31 – Other payables

As at 31 December 2016 and 2015, the caption "Other payables" is detailed as follows:

	2016		2015	
	Current	**Non-current**	**Current**	**Non-current**
Accrued costs	204,333	104,843	173,171	82,981
Related parties (Note 56)	7,500	-	193	-
Fixed assets suppliers	6,047	-	1,371	-
Personnel	5,675	-	3,668	-
Unions	283	-	292	-
Other	91,032	636	72,265	1,038
	314,870	**105,479**	**250,960**	**84,019**

✈ Accrued Costs

As at 31 December 2016 and 2015, the caption "Accrued costs" is detailed as follows:

	2016		2015	
	Current	**Non-current**	**Current**	**Non-current**
Remunerations	77,669	-	64,054	-
Maintenance reserves	22,569	104,843	14,416	82,981
Navigation charges	12,348	-	13,082	-
Aircraft fuel	11,313	-	12,834	-
Special sales charges	10,360	-	7,604	-
Remuneration - air crew	9,345	-	7,235	-
Variable remunerations	6,425	-	5,787	-
Booking fees	4,849	-	566	-
Maintenance and repair of materials	3,461	-	7,213	-
Handling services	2,868	-	3,841	-
Specialised w ork	2,867	-	3,706	-
Passenger boarding taxes	2,134	-	3,015	-
Insurance payable	1,361	-	3,304	-
Landing charges	1,321	-	601	-
Other	35,443	-	25,913	-
	204,333	**104,843**	**173,171**	**82,981**

The increase verified in maintenance is due, essentially, to the sale and leaseback operation of 3 aircrafts A330 that occurred during the first half of 2016, for the average period of 3 years, which represented an increase of contractual obligations at this date.

The special sales charges refer to commissions granted to agents according to the flight revenue for the year obtained through this sale channel.

✈ **Other - non-current**

As at 31 December 2016 and 2015, this caption refers to the fair value of the derivative financial instruments (interest rate swaps), in the amount of Euro 636 thousand and Euro 1,038 thousand, respectively (Notes 24 and 58).

✈ **Other - current**

As at 31 December 2016 and 2015, the caption "Other - current" was detailed as follows:

	2016	2015
Rates and taxes	72,461	56,779
Work accident indemnities	877	782
Other	17,694	14,704
	91,032	**72,265**

The caption of rates and taxes refers, essentially, to amounts payable to several entities, related to rates charged to customers on the issued tickets. The variation observed is related to the variation of the caption liabilities from unused flight documents due to the increase in the number of tickets issued in the second half of the year when compared to the same period of the previous year.

32 – Liabilities from unused flight documents

As at 31 December 2016 and 2015, the Group's liabilities relative to unused flight documents were as follows:

	2016	2015
Passengers	317,317	270,516
Cargo	550	552
	317,867	**271,068**

The variation verified in this caption is related to the joint effect of the increase of the timing of anticipation of purchase date when compared to the flight date and the increase in the number of tickets sold.

During 2016 and 2015, based on the partial and periodic analyses of this heading (Note 2.27.), adjustments were made to the revenue from passenger and cargo transport in the amount of Euro 74,553 thousand (3.5% of revenue from flown tickets) and Euro 73,214 thousand (3.3% of revenue from flown tickets), respectively, which were recognised under the caption "Sales and services rendered".

35 - Sales and services rendered

As at 31 December 2016 and 2015, the sales and services rendered, by external and internal market, are presented as follows:

	2016	2015
Sales		
Internal market		
Air transport and maintenance	419	391
Catering	6,193	5,910
Health care	155	136
Other	1,373	1,382
External market		
Air transport and maintenance	29,056	18,576
	37,196	**26,395**
Services rendered		
Internal market		
Air transport and maintenance	163,910	129,510
Catering	2,492	2,242
Health care	3,342	3,307
Information technologies	1,744	1,035
Other	4,677	3,870
External market		
Air transport and maintenance	2,076,277	2,242,363
	2,252,442	**2,382,327**
	2,289,638	**2,408,722**

The breakdown of sales and services rendered by geographic market is as follows:

2016	Air Transport	Maintenance Portugal	Maintenance Brazil	*Catering*	Holdings and other	Consolidated
Sales and services rendered:						
Mainland Portugal and islands	150,712	13,617	-	8,685	11,291	184,305
Europe	880,860	38,567	-	-	-	919,427
South Atlantic	586,150	8,288	81,248	-	-	675,686
North Atlantic	176,512	9,805	-	-	-	186,317
Mid Atlantic	31,309	-	-	-	-	31,309
Africa	284,854	569	-	-	-	285,423
Other	-	7,171	-	-	-	7,171
	2,110,397	**78,017**	**81,248**	**8,685**	**11,291**	**2,289,638**

2015	Air Transport	Maintenance Portugal	Maintenance Brazil	*Catering*	Holdings and other	Consolidated
Sales and services rendered:						
Mainland Portugal and islands	114,830	15,071	-	8,152	9,730	147,783
Europe	854,196	72,796	-	-	-	926,992
South Atlantic	728,516	2,415	62,666	-	-	793,597
North Atlantic	124,900	3,426	-	-	-	128,326
Mid Atlantic	68,505	-	-	-	-	68,505
Africa	335,749	1,385	-	-	-	337,134
Other	148	6,237	-	-	-	6,385
	2,226,844	**101,330**	**62,666**	**8,152**	**9,730**	**2,408,722**

Sales and services rendered by geographic market are defined based on the destination country of the goods and services rendered by the Group, which, in the case of air transport, is considered the destination country of the flight.

36 - Operating government grants

For the years ended as at 31 December 2016 and 2015, this caption amounts Euro 1,106 thousand and Euro 594 thousand, respectively.

37 - Gains and losses in associates

For the years ended as at 31 December 2016 and 2015, the caption of gains and losses in associates are detailed as follows:

	2016	2015
Gains		
SPdH	1,743	1,067
	1,743	**1,067**

The amount recorded in this caption at 31 December of 2016 and 2015, amounting to Euro 1,743 thousand and Euro 1,067 thousand, respectively, refers to the appropriation of the Group's share in the net income of the company SPdH (Nota 26).

38 - Variation in production

The variation in production in 2016 and 2015 was as follows:

	2016	2015
Inventories - opening balance (Note 20)	(5,545)	(14,173)
Adjustment of inventories	(5)	39
Inventories - closing balance (Note 20)	7,870	5,545
	2,320	**(8,589)**

39 – Internally generated assets

Internally generated assets, in 2016 and 2015, in the amount of Euro 559 thousand and Euro 608 thousand, respectively, refer essentially to personnel and other costs included in the acquisition cost of inventories (Note 5).

40 - Cost of goods sold and materials consumed

The cost of goods sold and materials consumed in 2016 and 2015 was as follows:

	2016		2015	
	Goods	Raw, subsidiaries and consumable materials	Goods	Raw, subsidiaries and consumable materials
Inventories - opening balance (Note 20)	16,719	108,125	15,112	117,319
Purchase goods	5,603	156,592	22,337	126,864
Transfer to non-current assets held for sale (Note 23)	(17,194)	(14)	(16,648)	(19)
Adjustment of inventories	-	3,629	(5)	(12,945)
Inventories - closing balance (Note 20)	(64)	(127,001)	(16,719)	(108,125)
	5,064	**141,331**	**4,077**	**123,094**
		146,395		**127,171**

The cost of goods sold and materials consumed has increased 12% in 2016, when compared to last year, due to the increased consumption of materials in maintenance and engineering activities in Portugal, despite the decrease in activity for third parties, due to the fact that the activity for the company itself increased, namely with the 11 phase-in of the year 2016, which resulted in significant consumption of materials for aircraft adaptation and modification.

In 2016 and 2015, the caption “Adjustment of inventories” refers, essentially, to the currency translation differences, verified in the Brazilian subsidiary, denominated in Reals, and to the capitalization of own fleet maintenance.

41 - External supplies and services

External supplies and services are detailed as follows:

	2016	2015
Aircraft fuel	433,819	660,310
Handling services	153,292	154,337
Navigation charges	141,847	151,730
Operating leases of aircraft and spare parts	118,862	77,595
Maintenance and repair of flight equipment	115,165	102,474
Specialised w ork	108,323	93,952
Landing charges	76,362	74,233
Rental costs	46,523	50,296
In-flight expenses	34,475	36,271
Commissions	28,023	26,679
Special sales charges - air transport	23,537	25,255
Accommodation and meals during stopovers	16,702	17,555
Subcontracts	16,343	16,417
Maintenance and repair of other assets	14,876	14,456
Fees	6,196	6,231
Insurance	5,828	6,834
Surveillance and security	3,023	2,848
Other costs related to external supplies and services	167,916	146,909
	1,511,112	**1,664,382**

The caption "Other costs related to external supplies and services" presents the following detail:

	2016	2015
Other costs related to passengers	24,989	25,899
Air traffic control charges	22,635	20,749
Facilities at airports	22,243	16,896
Advertising and publicity	21,198	13,573
Chartering of aircraft	21,009	13,934
Baggage, cargo and mail charges	13,768	16,272
Ground costs related to executive class passengers	8,850	7,409
Communication	6,970	7,528
Transport of goods	4,821	4,338
Electricity	4,455	4,491
Cleaning, hygiene and comfort	3,610	3,594
Travel costs	3,287	2,898
Other	10,081	9,328
	167,916	**146,909**

The decrease in external supplies and services expenses is mainly due to the decrease in fuel expenses, considering the effect of the reduction in the average jet fuel price and the fact that in 2015 losses were recognised for financial derivative instruments contracted in 2014, which caused losses of Euro 80 million in 2015, which hasn’t occurred in 2016 (see Note 3).

The increase in operating leases expenses is justified by the increase in the average number of aircrafts under operating lease, specifically the fact that, at the end of the year 2015, 6 A319 aircrafts were included in this lease scheme, the inclusion during the 2016 of 9 Embraer 190 aircrafts, 5 A330 aircrafts, and the formalisation of an ACMI contract with White for 8 ATR 72-600 aircrafts (Note 5).

42 - Employee costs

Employee costs are detailed as follows:

	2016	2015
Employee remuneration	438,935	421,855
Social Security Contributions	88,208	84,606
Other personnel costs	51,819	43,105
Expenses related to post-employee benefits obligation (Note 28)	6,869	7,391
	585,831	**556,957**

The increase in employee costs is mainly due to the restitution of employee seniorities and the compensation of pilots and cabin crew verified in 2016.

The remunerations attributed to the Statutory Bodies, in 2016 and 2015, were:

	2016	2015
Board of Directors (Note 56)	2,315	2,261
General Meeting	-	3
Supervisory Board / Statutory Auditor	93	11
	2,408	**2,275**

The caption "Other personnel costs" is detailed as follows:

	2016	2015
Insurance	19,178	19,493
Social action costs	10,329	10,036
Indemnities	7,811	3,111
Meals allowance	5,032	5,015
Training	4,656	1,094
Other	4,813	4,356
	51,819	**43,105**

43 – Impairment in inventory (losses/reversals)

For the years ended as at 31 December 2016 and 2015, this caption is detailed as follows:

	2016		2015	
	Inventory impairment	Reversal of inventory impairment	Inventory impairment	Reversal of inventory impairment
Raw materials, inputs and consumables (Note 20)	2,643	(831)	533	(739)
	2,643	**(831)**	**533**	**(739)**
		1,812		**(206)**

44 - Impairment in receivables (losses/reversals)

For the years ended as at 31 December 2016 and 2015, this caption is detailed as follows:

	2016		2015	
	Impairment of receivables	Reversal of impairment of receivables	Impairment of receivables	Reversal of impairment of receivables
Trade receivables (Note 21)	4,485	(2,399)	6,908	(1,363)
Other receivables - current (Note 18)	73	(30)	143	(33)
	4,558	**(2,429)**	**7,051**	**(1,396)**
		2,129		**5,655**

45 - Provisions (increases/decreases)

For the years ended as at 31 December 2016 and 2015, this caption is detailed as follows:

	2016	2015
Provision for legal claims (Note 26)	(468)	(370)
Other provisions (Note 26)	(974)	200
	(1,442)	**(170)**

46 - Impairment of assets subject to depreciation/amortisation (losses/reversals)

In 2016 an impairment loss was recognised in the subsidiary Portugália relating to its aircrafts in the amount of Euro 2,294 thousand, considering the valuations obtained. Should be noted that this fleet is not in operation given the fleet renewal occurred in 2016 (see Note 3).

47 - Fair value increases/reductions

During the year ended on 31 December 2016, a gain of Euro 32 thousand was recognised (2015: a loss of Euro 174 thousand) related with changes in fair value of investment properties (Note 6).

48 – Other operational income

For the years ended as at 31 December 2016 and 2015, the caption other operational income is detailed as follows:

	2016	2015
Supplementary income	24,630	37,593
Gains from tangible fixed assets	16,851	25,628
Currency translation differences	3,836	-
Gains from inventories	232	83
Cash discounts received	107	140
Other income and gains	135	977
	45,791	**64,421**

The caption "Supplementary income" presents the following composition as at 31 December 2016 and 2015:

	2016	2015
Recovered w arehouse material	5,536	8,660
Sale of miles	3,186	8,547
Rents and sub-leases	2,784	2,881
Advertising	2,610	3,766
Other	10,514	13,739
	24,630	**37,593**

The variation in gains from tangible fixed assets is mainly due to the gain resultant from the disposal of three A330 aircrafts in a sale and leaseback operation during the first half of 2016, amounting to Euro 16,261 thousand (Note 5), compared to the capital gain in 2015 from the sale of six A319 aircrafts in the amount of Euro 24,207 thousand.

49 - Other operational costs

For the years ended as at 31 December 2016 and 2015, the caption other operational costs is detailed as follows:

	2016	2015
Taxes	9,280	10,210
Other costs and losses from financial services	6,079	5,448
Indemnities from legal claims	4,151	2,896
Losses from tangible fixed assets	1,591	2,621
Inventory losses	820	1,364
Fines and penalties	191	484
Currency translation differences	-	51,125
Other	3,000	2,809
	25,112	**76,957**

During 2015 the costs on currency translation differences resulted from the combined effect of the depreciation of the Brazilian Real and appreciation of the dollar in respect of the Euro.

50 - Depreciation and amortisation costs

For the years ended as at 31 December 2016 and 2015, this caption is detailed as follows:

	2016	2015
Tangible fixed assets (Note 5)		
Buildings and other constructions	5,689	5,748
Basic equipment	46,513	53,436
Transport equipment	296	166
Tools and utensils	887	998
Administrative equipment	1,079	1,062
Other tangible fixed assets	210	191
	54,674	**61,601**
Intangible assets (Note 8)		
Intangible assets	228	250
	228	**250**
	54,902	**61,851**

Depreciation and amortisation expenses reduced by 11% in 2016, mainly as a result of the reduction in the number of aircrafts owned by the TAP Group or acquired under a financial leasing (Note 5).

51 – Finance Income and Costs

For the years ended as at 31 December 2016 and 2015, this captions are detailed as follows:

	2016	2015
Income and gains		
Interest income from investments	2,877	4,631
	2,877	**4,631**
Costs and losses		
Interest costs on loans	39,640	42,966
Currency translation differences	2,734	20,143
Other financial costs and losses	1,816	4,795
	44,190	**67,904**

The amount of interest costs on loans is net of capitalised interest on tangible fixed assets (Euro 6,890 thousand as of 31 December 2016).

The unfavourable currency translation differences in 2015 resulted essentially from the significant appreciation of the US Dollar during that period.

52 – Income tax for the year

The Group's companies with head office in Portugal are subject to Corporate Income Tax (IRC) based on their individual net income, at the rate of 21% plus a surcharge at the maximum rate of 1.5% on taxable profit, thus reaching an aggregate rate of 22.5%. This rate is increased by 3% on the portion of taxable profit of each company which is greater than Euro 1.5 million and less than Euro 7.5 million, by 5% on the portion of taxable profit of each company which is greater than Euro 7.5 million and less than Euro 35 million, and by 7% on the portion of taxable profit of each company which is greater than Euro 35 million, giving rise to an aggregate maximum tax rate of 29.5%.

In the calculation of the taxable profits, to which the tax rates referred to above are applied, the amounts not accepted for tax purposes are added and subtracted to the accounting results. These differences between the results for accounting and tax purposes may have a temporary or permanent nature.

Under the terms of article 88 of the Corporate Income Tax Code, the Group's companies based in Portugal are subject to autonomous taxation on some expenses, at the tax rates listed therein.

In accordance with the legislation in force, the tax returns of companies, placed in Portugal, included in the consolidation, are subject to review and correction by the tax authorities for a period of four years (five years for Social Security), except when tax losses have occurred, tax benefits have been granted, or inspections, claims or challenges are in course, in which cases, depending on the circumstances, the periods are extended or suspended. The Board of Directors of the Group understands that any corrections resulting from revisions/inspections by the tax authorities to those tax returns will not have a significant effect on the consolidated financial statements as of December 31, 2016 and 2015.

For the year ended as at 31 December 2016 and 2015, the caption "Income tax for the year" is detailed as follows:

	2016	2015
Current tax	486	9,735
Deferred tax (Note 15)	3,202	(29,911)
	3,688	**(20,176)**

The reconciliation of the effective tax rate for 2016 and 2015 is detailed as follows:

	2016	2015
Net income/(loss) before income tax	**(28,269)**	**(180,615)**
Nominal tax rate	21%	21%
	(5,936)	**(37,929)**
Permanent differences	7,346	6,175
Insufficient/(surplus) estimate of taxes for the previous year	(595)	1,397
Use of tax losses carried forward of previous years without DTA	(9)	-
Tax losses carried forward for the year without DTA	2,590	2,253
Autonomous taxation and other forms of taxation	292	7,928
Income tax	**3,688**	**(20,176)**
Effective tax rate	(13%)	11%

53 - Non-controlling interests - net income

The non-controlling interests, presented in the consolidated income statement, as at 31 December 2016 and 2015 are detailed as follows:

	2016	2015
Non-Controlling interests of net income		
TAP ME Brasil	(473)	(546)
Cateringpor	808	567
LFP	4,383	4,244
	4,718	**4,265**

54 – Non-recurring items

In the context described in Note 22, as at 31 December 2015, the Board of Directors considered that the best estimate for the exchange rate of cash held in Venezuela is the SIMADI rate, which resulted in the recognition of a negative exchange variation in the amount of Euro 91,394 thousand, recorded under this caption, since it reflects a situation considered as non-recurring, considering its nature and magnitude in the context of these consolidated financial statements.

55 - Segment reporting

The following business segments have been identified: air transport, maintenance, catering and other. The net income/(loss) of each segment correspond to those directly allocated to them, as well as to those that can be reasonable attributed to those segments.

The financial information by operational segment for 2016 is analysed as follows:

	Air Transport	Maintenance		*Catering*	Holdings and other	Intersegment eliminations	Consolidated
		Portugal	Brazil				
REVENUE							
Revenue	2,110,464	79,132	84,091	48,818	54,246	(87,113)	2,289,638
Net operating income/(loss)	34,973	8,699	(16,747)	2,065	(15,946)	-	13,044
External net financial results	(4,781)	-	(18,009)	(19)	(18,504)	-	(41,313)
Net gains in associates	-	-	-	-	1,743	-	1,743
Income tax	(942)	-	-	(497)	(2,249)	-	(3,688)
Non-controlling interests	-	-	(473)	808	4,383	-	4,718
Net income/(loss) for the year from continuing operations	**29,250**	**8,699**	**(34,756)**	**1,549**	**(36,699)**	**-**	**(31,957)**

The financial information by operational segment for 2015 is analysed as follows:

	Air Transport	Maintenance Portugal	Maintenance Brazil	*Catering*	Holdings and other	Intersegment eliminations	Consolidated
REVENUE							
Revenue	2,226,998	102,021	68,611	46,652	50,064	(85,624)	2,408,722
Net operating income/(loss)	(99,762)	10,881	(17,061)	1,585	(12,985)	-	(117,342)
External net financial results	(2,131)	-	(23,102)	10	(38,050)	-	(63,273)
Net gains in associates	-	-	-	-	1,067	-	1,067
Income tax	(7,754)	-	-	(437)	28,367	-	20,176
Non-controlling interests	-	-	(546)	567	4,244	-	4,265
Net income/(loss) for the year from continuing operations	**(109,647)**	**10,881**	**(40,163)**	**1,158**	**(22,668)**	**-**	**(160,439)**

56 - Related parties

Balances and transactions between Group companies which are included in the consolidation perimeter are eliminated in the consolidation process, and, therefore, are not disclosed in the present Note. The balances and transactions between the Group and the related parties are presented below. The terms and conditions enforced between the Group and the related parties are similar in substance to the terms which would normally be contracted between independent entities in comparable operations.

The members of the Group's Board of Directors were considered, according to IAS 24, as the only "key" management members of the Group.

During the financial years ended on 31 December 2016 and 2015, the remunerations earned by the Board of Directors and by the General and Supervisory Board reached Euro 2,315 thousand (2015: Euro 2,261 thousand), as described in Note 42.

As at 31 December 2016 and 2015, the balances with related parties are detailed as follows:

	2016 - Assets			
	Other receivables non-current (Note 18)	Trade Receivables (Note 21)	Other receivables non-current (Note 18)	Deferrals
Associates				
SPdH - Serviços Portugueses de Handling, S.A.	4,700	729	688	-
Other related entities				
Azul S.A.	4,744	1,436	575	731
	9,444	**2,165**	**1,263**	**731**

	2016 - Liabilities			
	Borrowings non-current (Note 27)	Suppliers (Note 30)	Other payables current (Note 31)	Deferrals
Shareholders				
Atlantic Gateway, SGPS, S.A.	-	(76)	-	-
Parpública - Participações Públicas, SGPS, S.A.	(31,249)	-	-	-
Associates				
SPdH - Serviços Portugueses de Handling, S.A.	-	(795)	(6,665)	(99)
Other related entities				
Azul S.A.	(94,754)	(1,045)	(835)	-
	(126,003)	**(1,916)**	**(7,500)**	**(99)**

	2015 - Assets			
	Other receivables non-current (Note 18)	Trade Receivables (Note 21)	Other receivables non-current (Note 18)	Deferrals
Associates				
SPdH - Serviços Portugueses de Handling, S.A.	4,700	1,157	106	-
	4,700	**1,157**	**106**	**-**

	2015 - Liabilities			
	Borrowings non-current (Note 27)	Suppliers (Note 30)	Other payables current (Note 31)	Deferrals
Associates				
SPdH - Serviços Portugueses de Handling, S.A.	-	(6,862)	(193)	(100)
	-	**(6,862)**	**(193)**	**(100)**

For the years ended as at 31 December 2016 and 2015, the transactions with related parties are as follows:

	2016				
	External supplies and services	Other operational costs	Sales and services rendered	Other operational income	Financial results
Shareholder					
Atlantic Gateway, SGPS, S.A.	(663)	-	-	-	-
Parpública - Participações Públicas, SGPS, S.A.	-	-	-	-	(1,249)
Associates					
SPdH - Serviços Portugueses de Handling, S.A.	(79,738)	(32)	6,599	1,231	-
Other related entities					
Azul S.A.	(16,727)	(4,038)	587	-	(4,754)
	(97,128)	**(4,070)**	**7,186**	**1,231**	**(6,003)**

	2015				
	External supplies and services	Other operational costs	Sales and services rendered	Other operational income	Financial results
Associates					
SPdH - Serviços Portugueses de Handling, S.A.	(77,614)	(8)	6,592	1,235	89
	(77,614)	**(8)**	**6,592**	**1,235**	**89**

The transactions, amounting to the total of Euro 79,738 thousand (2015: Euro 77,614 thousand) recorded under external supplies and services, refer to ground handling services provided by SPdH to support aircraft, passengers, baggage, cargo and mail.

57 - Contingencies

Contingent assets

As at 31 December 2016 and 2015, the Group have no contingent assets.

Contingent liabilities

The Brazilian subsidiary TAP M&E Brasil is involved in tax, civil and labour claims, involving risks of loss classified by the Board of Directors as possible, based on the appraisal of its legal consultants, for which no provision has been recognised, as follows:

✈ **Labour claims**

(i) Dangerousness/ Insalubrity and Other
Amount: Euro 75,416 thousand

The main labour claim refers to the request for additional payment due to insalubrity and hazard, for all employees working as aircraft maintenance auxiliaries at Porto Alegre. Following analysis of the expert's report, it was concluded that the activities exercised are not characterised as hazardous or insalubrious. The Union has filed an appeal which is currently at the Superior Labour Court of Brasília pending judgement.

Other actions relate to individual cases concerning claims of different kinds, such as overtime, moral damages, among others.

Based on information provided by its lawyers, TAP M&E Brasil understands that from these legal actions will not result material impacts on its financial statements as at 31 December 2016.

✈ **Tax claims**

(ii) Notice of infraction of import tax (“II”), tax on industrialised products (“IPI”), PIS and COFINS
Amount: Euro 25,456 thousand

The subsidiary was notified by the Federal Reserve Office, on 26 April 2010, which considered that the exemption of II and IPI and 0% rate of PIS and COFINS are not applicable to the import operations of the subsidiary. The subsidiary's challenge has been filed and awaits trial.

Based on information provided by its lawyers, TAP M&E Brasil understands that from this legal action will not result material impacts on its financial statements as at 31 December 2016.

(iii) Tax foreclosure relative to accessory obligations of tax on circulation of goods and services ("ICMS")
Amount: Euro 9,932 thousand

In December 2007, the subsidiary was notified, in the context of tax foreclosure, proposed by the State Treasury Office of São Paulo (Guarulhos), relative to accessory obligations of ICMS. The subsidiary pledged 2% of turnover, and suspended the foreclosure, arguing for a review of the tax foreclosure. The subsidiary is currently awaiting the Judge's decision relative to the suspension of the foreclosure.

(iv) Notice of infraction regarding failure to comply with the temporary import regime.
Amount: Euro 7,191 thousand

In 2012, the subsidiary was notified by the Federal Revenue Office, due to failure to comply with the temporary import regime. The subsidiary awaits judgement of the appeal filed with the Tax Appeals Administration Board ("CARF"). In September 2016 the subsidiary Voluntary Appeal was not accepted by CARF and the notice of inspection was partially revoked.

(v) Notice of infraction of PIS and COFINS - 2006
Amount: Euro 3,416 thousand

The tax authorities considered that there were differences between the analytical ledger and the Declaration of federal tax debits and credits ("DCTF"), with reference to 2006. The subsidiary allegations were not considered by CARF, and new declarations were filed, which are waiting judgement.

(vi) Notice of infraction of PIS and COFINS - 2007
Amount: Euro 1,701 thousand

The federal tax authorities considered that there was inconsistency in the statements presented by the subsidiary regarding PIS and COFINS contributions. A protest letter has been submitted in 2012 and trial is pending at first instance.

(vii) Notice of infraction of "ICMS"
Amount: Euro 1,329 thousand

TAP M&E Brasil was notified in 2014 by the Secretary of the Treasury Office of Rio Grande do Sul, due to the ICMS credit on electricity in Porto Alegre. The subsidiary filed a challenge and is still awaiting for trial.

✈ **Civil claims**

(viii) Claims over lawyers' fees
Amount: Euro 3,224 thousand

Claims over fees filed by a law firm against the subsidiary TAP M&E Brasil, within the scope of the withdrawal of the lawsuit and adhesion to the subdivision programme of REFIS. It is currently awaiting judgement of the appeal.

✈ **Other**

(ix) Pledged assets
Amount: Euro 14,310 thousand

The subsidiary TAP M&E Brasil has pledged various assets in the amount of Euro 4,310 thousand, which refer to guarantees required in tax and labour proceedings. These assets include vehicles, computers, components and items of the hangars of Rio de Janeiro and Porto Alegre, among others.

TAP SGPS and TAP SA were notified on 10 November 2016 by a "Notice of Objections" issued by the European Commission – Directorate General for Competition, concerning the fares charged by TAP SA and SN Brussels on the Lisbon-Brussels route, considering the existing code-share agreements. TAP Group presented its defence in 2017 and understands that there are no substantiated indications of any breach and therefore an outflow of resources is not probable to be required.

Pledged Guarantees

As at 31 December 2016 and 2015, the pledged guarantees by the Group are detailed as follows:

	2016	2015
Bank guarantees provided by TAP S.A.		
Aircraft	47,357	45,874
Natwest - Acquiring relative to credit cards	2,453	2,861
Fuel	2,199	3,019
Portuguese State - Operation of the Azores routes	1,654	1,654
Labour Court	1,053	1,329
Other	15,443	11,170
Bank guarantees provided by LFP		
Operating license concession contracts for Lojas Francas	11,724	9,000
Bank guarantees provided by other Group companies	2,057	397
Securities provided to insurers	90	90
	84,030	**75,394**

The actual guarantees provided under finance agreements are disclosed in Note 27.

58 - Financial assets and liabilities

The reconciliation of the consolidated financial positions, as at 31 December 2016 and 2015, relative to the different categories of the financial assets and liabilities, are detailed as follows:

	2016				
	Derivative financial instruments classified as hedge instruments (Note 24)	Credit and other receivables	Other assets/financial liabilities	Non-financial assets and liabilities	Total
Assets					
Other non-current assets	-	81,175	39,654	-	120,829
Current receivables	-	260,430	-	40,281	300,711
Restricted cash	-	538	-	-	538
Cash and cash equivalents	-	150,468	-	-	150,468
Total Assets	**-**	**492,611**	**39,654**	**40,281**	**572,546**
Liabilities					
Non-current borrow ings	-	-	(666,841)	-	(666,841)
Other non-current liabilities	(636)	-	(104,843)	-	(105,479)
Current borrow ings	-	-	(328,274)	-	(328,274)
Current payables	-	-	(467,956)	(421,359)	(889,315)
Total Liabilities	**(636)**	**-**	**(1,567,914)**	**(421,359)**	**(1,989,909)**

	2015				
	Derivative financial instruments classified as hedge instruments (Note 24)	Credit and other receivables	Other assets/financial liabilities	Non-financial assets and liabilities	Total
Assets					
Other non-current assets	-	50,952	-	-	50,952
Current receivables	-	202,326	-	30,699	233,025
Restricted cash	-	4,177	-	-	4,177
Cash and cash equivalents	-	136,814	-	-	136,814
Total Assets	**-**	**394,269**	**-**	**30,699**	**424,968**
Liabilities					
Non-current borrow ings	-	-	(743,370)	-	(743,370)
Other non-current liabilities	(1,038)	-	(82,981)	-	(84,019)
Current borrow ings	-	-	(198,797)	-	(198,797)
Current payables	-	-	(420,062)	(357,665)	(777,727)
Total Liabilities	**(1,038)**	**-**	**(1,445,210)**	**(357,665)**	**(1,803,913)**

The following tables present the assets and liabilities measured at fair value as at 31 December 2016 and 2015, according to the following fair value hierarchical levels established in IFRS 13:

Level 1: the fair value of financial instruments is based on prices available on active, liquid markets at the date of the financial position;

Level 2: the fair value of financial instruments is not determined based on active market prices, but rather through valuation models. The main inputs of these models are observable on the market; and

Level 3: the fair value of financial instruments is not determined based on active market prices, but rather through valuation models, whose main inputs are not observable on the market.

✈ Assets measured at fair value

	2016		
	Level 1	Level 2	Level 3
Non-financial assets			
Investment properties	-	2,248	-

	2015		
	Level 1	Level 2	Level 3
Non-financial assets			
Investment properties	-	2,216	-

✈ Liabilities measured at fair value

	2016		
	Level 1	Level 2	Level 3
Financial liabilities			
Derivative financial instruments hedging	-	636	-
Non-financial liabilities			
Deferrals - Customers loyalty program	-	42,972	-

	2015		
	Level 1	Level 2	Level 3
Financial liabilities			
Derivative financial instruments hedging	-	1,038	-
Non-financial liabilities			
Deferrals - Customers loyalty program	-	41,995	-

Derivative financial instruments

The fair value of the derivative financial instruments is recorded under the caption of other payables when negative, and under the caption of other receivables when positive.

During 2016 and 2015, the variation of derivative financial instruments fair value was recognised in equity.

The breakdown of the derivative financial instruments fair value is detailed in Note 24.

Credit and other receivables

Other receivables are initially recognised at their fair value, corresponding to their nominal value, deducted of any impairment loss identified during credit risk analysis.

Other financial liabilities

Other financial liabilities are recognised at their amortised cost, corresponding to the amount of the respective cash flow, discounted by the effective interest rate associated to each liability.

60 - Commitments

✈ Purchase commitments

The acquisition of 53 aircrafts (39 A320 NEO Family and 14 A330 NEO) to be received between 2018 and 2025 is contracted with Airbus SAS ("Airbus"). This order is due to the novation to Transportes Aéreos Portugueses, SA of the previously negotiated acquisition agreement and signed between Airbus and DGN Corporation.

A commitment was also signed with CFM International Inc. on the acquisition of 83 LEAP-A1 reactors, including 5 reserve reactors, which will equip the new fleet of A320 NEO Family aircrafts.

✈ Other commitments

Once the need to add several aircrafts was identified, during 2017, both for replacement and for compliance with the scheduled expansion of the network, several commitments were signed during the last quarter of the year with several entities, namely with regard to the incorporation in the fleet of TAP SA of 1 A321-200, 1 A320-200 and 3 A330-300.

An intent letter was also signed in December 2016, establishing the conditions for the financing of pre-delivery payments to Airbus, in respect of some of the aircraft listed in the above mentioned acquisition agreement, with subsequent operating lease to TAP SA. An intent letter incorporating 4 A330-900 and 1 A320Neo was also signed in February 2017, with 2 of the A330-900 aircraft currently under the purchase agreement signed between Airbus and TAP SA, including the financing of the advances to be made to Airbus as pre-delivery payments.

As of 31 December 2016, there were financial commitments, assumed by the TAP Group, related to operating leases of aircrafts and reactors, in the amount of Euro 435,539 thousand (Euro 342,014 thousand at 31 December 2015) (Note 27).

61 - Subsequent events

Following the resolution of the Board of Directors of ANAC dated 23 December 2016, on 12 January 2017, the General Meeting of TAP SGPS resolved to recognise the full production of the effects of the bonds issued by TAP SGPS, which was approved by the General Meeting of TAP SGPS on 8 March 2016, as well as the effects of the guarantee agreement entered into under the aforementioned bond issuance between TAP SGPS, TAP SA, Megasis - Sociedade de serviços de Engenharia e Informática, S.A., Azul S.A. and Bondholders, SL. It should be noted that the TAP Group has not yet fulfilled the contractually agreed guarantees and agreed with the bond underwriters of an extension of the term for those guarantees.

In addition, since the beginning of 2017, Atlantic Gateway and Parpública have been working together with the TAP Group on the suspensive conditions established in the Share Purchase Agreement, in order to allow, in the short term, the conclusion of the transaction provided for in the same agreement, as a result of which Parpública is to become the holder of 50% of the share capital of TAP SGPS.

62 - Note added for translation

The accompanying financial statements are a translation of financial statements originally issued in Portuguese. In the event of any discrepancies the Portuguese version prevails.

CHARTERED ACCOUNTANT

Sandra Candeias Matos da Luz

BOARD OF DIRECTORS

Humberto Manuel dos Santos Pedrosa
Chairman

Fernando Abs da Cruz Souza Pinto
Member

David Humberto Canas Pedrosa
Member

Maximilian Otto Urbahn
Member

David Gary Neeleman
Member

Philippe Calixte Albert Delmas
Member

Sydney John Isaacs
Member

Robert Aaron Milton
Member

Henri Courpron
Member

Tiago Gonçalves de Aires Mateus
Member

Francisco Maria Freitas de Morais Sarmento Ramalho
Member