

Q1 2020 Earnings Call

Company Participants

- Abhi Manoj Shah, Chief Revenue Officer
- Alexandre Wagner Malfitani, Chief Financial Officer and Investor Relations Officer
- Andrea Bottcher, Investor Relations Manager
- David Gary Neeleman, Chairman of the Board
- John Peter Rodgerson, Chief Executive Officer

Other Participants

- Analyst
- Anezina Mytilinaiou
- Josh Milberg
- Matthew Wisniewski
- Michael Linenberg
- Pablo Monsivais
- Savanthi Syth
- Stephen Trent
- Victor Mizusaki

Presentation

Operator

Hello, everyone, and welcome to Azul's First Quarter 2020 Results Conference Call. My name is Beatrice, and I will be your operator for today. This event is being recorded and all participants will be in a listen-only mode until we conduct a question-and-answer session following the company's presentation. (Operator Instructions)

I would like now to turn the presentation over to Andrea Bottcher, Investor Relations Manager. Please proceed.

Andrea Bottcher {BIO 20316630 <GO>}

Thank you, Beatrice, and welcome all to Azul's first quarter earnings call. The results we announced this morning, the audio of this call and the slides that we'll reference are available on our IR website.

Presenting today will be David Neeleman, Azul's Founder and Chairman; and John Rodgerson, CEO. Alex Malfitani, our CFO; and Abhi Shah, our Chief Revenue Officer, are

also here for the Q&A session.

Before I turn the call over to David, I'd like to caution you regarding our forward-looking statements. Any matters discussed today that are not historical facts, particularly comments regarding the company's future plans, objectives and expected performance constitute forward-looking statements.

These statements are based on a range of assumptions that the company believes are reasonable, which are subject to uncertainties and risks that are discussed in detail in our CVM and SEC filings. Also during the course of this call, we will discuss non-IFRS performance measures, which should be -- should not be considered in isolation.

With that, I'll turn the call over to David. David?

David Gary Neeleman {BIO 687871 <GO>}

Thank you, Andrea. Hello, everybody, and thanks for joining us for our first quarter 2020 earnings call. As always, I want to start by thanking our crew members who are making great sacrifices to take care of our customers, each other and the company. Amazingly, almost 20 -- almost 80% of our crew members have elected to take unpaid leaves to help us all during this unprecedented time. This is an incredible number, and I'm very grateful for their support. It really speaks volumes about the amazing culture we have here at Azul.

Thanks to the team, we've created one of the best airlines in the world. We started this year as the largest airline in Brazil by a number of destinations. We are the number one airline with 83% of our markets -- we're number one in 83% of the markets we fly, one of the most profitable airlines in the world, and one of the carriers with the best customer service. It is certainly better to start a crisis from a position of strength and weakness.

The founding team at Azul has been with the company since the beginning. I have a CFO that I made the President, and that is very rare. Having two CFOs at the company in times like these is very important. I'd also like to take this opportunity to reaffirm the management team's and my full commitment to Azul long-term. There is nothing more important to me than Azul. It's such a great company.

What gives us all the greatest strength is the flexibility of its fleet, which you can see on Slide 4. We have anywhere from a nine-seater caravans all the way up to 214-seater 321s in our domestic fleet, which gives us enormous amount of flexibility as we go forward.

During times of uncertain demand, the best thing to do is to bring the demand in at the lowest possible trip costs. This is exactly what we are doing as we rebuild the network step-by-step. As demand recovers, we have more options to create -- to recreate our network than other airlines that have a larger single-type aircraft.

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Abhi is building the schedules on a weekly basis, which allows him to constantly test demand, swap out aircraft at different times. So if we can only fill an ATR with the demand, we fly an ATR. If he fills -- if we can fill an Embraer, we'll fly an Embraer. If he can fly with the 320 or a 321, we can fly that. This is why we've been able to grow our central network since April and continue to look for opportunities to keep it going. We are currently serving 38 destinations with 115 daily flights, and the revenue we are generating is enough to cover all of our variable costs if not higher.

Azul is fortunate to count on the support of many stakeholders including crew members, aircraft manufacturers and lessors, banks, suppliers and the Brazilian government. We have developed a recovery plan that includes a contribution from all of our stakeholders, and I'm confident that we will come out of this crisis stronger.

And with that, I'll pass it over to John, who will give you more details about first quarter results and our response to the crisis.

John Peter Rodgerson {BIO 17734009 <GO>}

Thanks David. I would also like to thank all of our crew members, our customers, partners and suppliers, and everyone who's contributing to protect Azul's long-term success. I'll give you a brief overview of our first quarter results, and then we will focus on the initiatives taken in response to the crisis.

Our revenues in the first quarter grew 10% year-over-year driven by strong passenger demand in January and February and a 12% growth in capacity. Azul came into this crisis strong with a stage-length adjusted unit revenue expansion in the first quarter, even with a significant increase of capacity.

In addition, our cargo business delivered another strong quarter of results with revenues up 41% year-over-year. Cargo continues to be a strategic business unit for Azul and we see a lot of potential for cargo in Brazil, especially in e-commerce. We recently adapted several passenger aircraft into cargo planes to be used during the crisis.

As you know with the implementation of travel restrictions and social distancing measures started in the second half of March, the Brazilian economy came to a standstill leading to a sharp drop in passenger demand. Our results were further impacted by the 18% depreciation of the Brazilian real. As a result, we recorded an EBIT of BRL170 million, representing a margin of 6.2%. Normalizing for currency and COVID-19, our EBIT margin would have been 14.9%.

As you can see on Slide 6, we ended the quarter with significant sources of liquidity in unencumbered assets, totaling over BRL6.7 billion. We have a strong balance sheet with no restricted cash. We also have our loyalty program, TudoAzul, which can sell points in advance and is wholly-owned and unencumbered.

The value of our investment have decreased to BRL937 million due to COVID-19. This amount includes the face value and accrued interest of the bond of approximately

BRL700 million. The bond is guaranteed by TAP who is expected to receive support from the Portuguese government. It's also secured by TAP's loyalty program. We will have the ability to convert this into cash.

Moving on to Slide 8. We moved quickly and aggressively to reduce our costs and improve our liquidity, while taking care of our customers and crew members. Since the onset of the pandemic, we reached -- we reacted quickly to make short-term adjustments to our network by cutting capacity by 50% in the second half of March.

On March 26, Azul was the first airline in Brazil to implement an essential air network, reducing its 950 daily departures to only 70. Since then, we've been carefully monitoring the demand recovery to gradually increase our network and schedules. It's important to highlight that we will only operate flights that generate enough revenue to cover its variable costs. This is why having a flexible fleet with the aircraft that have lower trip costs is key in the current environment.

Moving on to Slide 9. Our quick reaction to reduce capacity contributed to a significant reduction in variable cost, which represents approximately 60% of our operating expenses. In addition, we implemented several initiatives to reduce fixed cost, including an over 50% reduction in payroll in the second quarter, deferral of all aircraft lease payments, suspension of new aircraft deliveries, PDP payments and CapEx investments. Through the implementation of these initiatives, we significantly reduced our cash outflows.

Moving on to Slide 10. Our immediate response was -- has mainly been focused on preserving our financial liquidity to work through the crisis. We ended March with a cash position of BRL2.2 billion. In April, our cash actually went up and we expect to end the second quarter with approximately BRL2 billion in cash. We expect to have a net cash burn of only BRL3 million to BRL4 million a day in May and June. In addition, we have no PDP payments or aircraft CapEx commitments due in 2020. We have no significant debt repayments due this year.

Moving on to Slide 12. We've addressed the immediate cash needs and how -- and now have developed a recovery plan to continue to engage all stakeholders, including crew members, lessors, aircraft manufacturers, suppliers and government authorities to maintain the liquidity required to confront this crisis and optimize the airline for the future. This plan is based on conservative assumptions. We used to have the capacity to fly 1,000 flights a day in December, but we're planning for only 400 to be conservative in December.

As you can see on Slide 13, our plan is focused on several additional measures. We're looking at all payroll initiatives to adjust our fixed cost to the new demand environment. We're holding comprehensive renegotiations with the lessors to allow us to pay up as we increase our flight schedule. We're also seeking support from aircraft manufacturers and all OEMs. Yesterday, we announced the deferral of 59 E2 deliveries to 2024 and beyond.

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We have a great relationship with Embraer and are very excited about the E2. Unfortunately, we had to push back our plans to take on more of these planes until the economy recovers. It's important to highlight that we also have 51 aircraft naturally exiting our fleet before these E2s will arrive. This is excluding any potential subleases to LOT and Breeze, which still have signed contracts. To the extent that the market size changes post-COVID, we want to be prepared.

As mentioned before, we are no strangers to the short-term challenges and remain confident in our long-term targets. We entered this crisis as one of the strongest airlines in the world. Our fast response allowed us to build cash reserves for over one year. We're also taking conservative approach to demand recovery and have developed a plan to ensure a positive cash position in the long-term. And finally, our flexible fleet gives us a trip cost advantage that no other airline in the region has.

With that, David, Alex and I will take any of your questions.

Questions And Answers

Operator

(Question And Answer)

Ladies and gentlemen, thank you. We will now begin the question-and-answer session. (Operator Instructions) Our first question comes from Savi Syth, Raymond James.

Q - Savanthi Syth {BIO 17476219 <GO>}

Hey. Good afternoon. If I can ask just a little bit more clarity on the fleet plans. I think you were expecting about maybe 68 E2 by the end of 2023. And does this mean kind of you will only have kind of four more coming? Or just a little clarity on that. And then just to clarify, was the 51 aircraft that leaves over the next few years is that ex the E1?

A - John Peter Rodgerson {BIO 17734009 <GO>}

No. So Savi, just quickly. So we have -- there's four built Embraer aircraft that we're working through. They're going to a lessor and we're working through that with them. First of all, what we found out is the greatest asset that anybody can have in this crisis is an airline that can actually pay their bills, right? And so the asset values don't exist anymore. Not for 737, A320, E1 or anything. And so what everybody wants is for airlines to be healthy that can continue to pay.

So what we've decided to do is stop the incoming flow of aircraft and that was the big important step that we took, and so all aircraft that haven't been built yet will not come in. And then allow us to take down the fleet as we go forward over the next couple of years. The 51 aircraft that we mentioned is the natural redeliveries that we have, not that gets accelerated with LOT and Breeze. But a lot of people have question, is LOT and Breeze still on and they still have commitments with us. They will see take it, but every airline in the world is currently suffering.

So we wanted to give a conservative assumption on that. And so the 51 aircraft that are leaving are several different aircraft types. We have sealed -- we have A330 seals leaving. We have E1s leaving. We have ATRs leaving. We have 737 cargo planes leaving in that same period. And so what we've done is no new aircraft coming in from now until 2024 to give us the headroom in case the market is smaller in a post-COVID world.

Q - Savanthi Syth {BIO 17476219 <GO>}

And if things recover sooner, I'm guessing that are you able to kind of rework that? Or...

A - John Peter Rodgers {BIO 17734009 <GO>}

Yes, absolutely. I mean, I think that the aircraft manufacturers would certainly like to deliver aircraft sooner and we're working through plans with them. Savi, one other thing that I think is really important. A lot of the E2s that we were taking, the initial E2s were coming through lessors. And so the lessors were actually very happy because it reduces their CapEx in the short term and their financing risk associated with financing aircraft as well.

And so as we're looking for support in a step-up plan for our leases, that having the lessors taking a little bit of that burden off of them is great. And the other great thing is that we did this with no penalties. And so Embraer -- it's in Embraer's best interest to have a healthy Azul that will be able to take our full order in the future. And so we help the lessors. We help ourselves significantly in that process. And having that lessors healthier, it actually helps us as we look for their support as we move forward.

Q - Savanthi Syth {BIO 17476219 <GO>}

Makes sense. And just on that same topic, last question is just how are you thinking about it than CapEx? And, I know you gave some color on 2020. What would that look like in 2021?

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

I think it will be very much dependent on the recovery. If we have excess aircraft, we can stagger them and we can manage, so that we do not have to incur any heavy maintenance checks and we can fly the aircraft that have available time without kind of tripping up any big maintenance milestones. And then if we're flying all of the aircraft, that's a good problem to have, right? And then, we'll have the ability to perform those maintenance checks and we'll have the CapEx for it. But assuming the conservative scenario of demand recovery that we have assumed, you can assume no CapEx for the foreseeable future.

Q - Savanthi Syth {BIO 17476219 <GO>}

That's helpful. Thank you.

A - John Peter Rodgers {BIO 17734009 <GO>}

Thanks, Savi.

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Operator

Our next question comes from George Milberg, Morgan Stanley.

Q - Josh Milberg {BIO 19336060 <GO>}

Hey everyone. Thank you for the call and the questions. I wanted to first ask about your cash flow. When we had spoken to Alex around mid-April, I think you were indicating a monthly cash burn of BRL150 million to BRL200 million. And the new guidance implies a number that's considerably below that. I know that there are a lot of moving parts, but just wanted to better understand the specific variables behind the improvement, if I've got the numbers right.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

No. Hey Josh. I think you do. But, yes, we have seen an improvement from what we originally assumed and there are a lot of moving parts, like you said. I mean, one thing that's encouraging is that when we say that we're flying flights that cover their marginal cost, we're actually seeing that it covers -- it's not breakeven, right?

There is a good cushion there between the variable cost of the flight and the revenue that we are getting, right? And that's why you're also seeing a significant increase from the number of flight that we flew in April the number of flight that we're flying in May. Obviously, it's still a long way to go until we get back to the almost 1,000 flights a day that we used to fly. But that's part of it.

And we're also finding a lot of cash sources that we're working through. And some of these are under negotiations. Some of these we conservatively assumed that we wouldn't be able to get, but we were able to execute on them. So for example, kind of replacing cash collateral for insurance. So some of these initiatives which are outside of our control originally we didn't assume that we were able -- going to be able to tap them to be conservative, but we have been able to execute it upon them.

And also like John said, it's in our suppliers and lessors' best interest to support Azul in this period, because, the way for them to maximize their payout is for us to get to the other side, right, and have a healthy cash generating airline after this crisis. That's the best way -- that's the way that they will be doing the best favor for themselves. And that's what we've been seeing that, over time we've been able to get these stakeholders to support us in a stronger way than we originally expect.

Q - Josh Milberg {BIO 19336060 <GO>}

Okay. And as a part of that and talking about your stakeholders, it sounded like from your comments that you're a little further along in your agreements with lessors than you were a month ago. I think you mentioned that your payments would move in tandem with you're putting back the capacity. But can you talk a little bit more about that?

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

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Yes. That's a contract. In the conversations with the lessors are being very positive and again, very collaborative because it's the intersection of what's best for Azul and best for the lessors, right? It's not a sort of a zero-sum game here. If everybody helps us, we'll get to a cash generating position, everybody will benefit. So that's the

-- we don't want to commit to something that we can't deliver. And also the lessors know that it's not constructive for us to just promise them to pay them something that we're not able to pay. The best way for us to pay the lessors is to pay them as we start generating cash by operating, right? So that's the natural profile of what the payment should look like, because anything that deviates from that is just not realistic, right? And so we're still talking to most of our lessors. We have agreements with some of them as well.

But we believe that, with the tone of the conversations that we're having with the sharing of our plan, the conservatism of our cash recovery -- of our demand recovery plan, this is all kind of coalescing around the management recovery plan that we mentioned, which kind of aligns all stakeholders' interest and gets contributions from all of our stakeholders. Whatever it is that stakeholders want to do first is sure that this plan is the equitable, right?

The worst thing I think for a lessor is for them to pay more of the tab than the other lessor. But if you're treating all lessors fairly, they understand, right? They -- it's really the best way for themselves to get the maximum payout possible. And same thing among banks. Same thing among suppliers. Same thing among all of our stakeholders, right? It's treating kind of each category equitably and making sure that we get to the other side of this crisis.

A - John Peter Rodgerson {BIO 17734009 <GO>}

Hey Josh, I would just add a couple of things. 60 days ago, a lessor would call and say, "Hey, I want to get paid, I want to get paid." I want to get paid. Now they're calling and say, "how are we going to help," right? And I think it's completely changed the tone. I think the world has grounded airlines. And so everybody -- they are taking 10-12 year risk on Azul, right?

And I think that that's something that they need us to be healthy because, their asset has no -- doesn't have value right now. Their asset is the airline customers that can pay them. And so I think, had we cut deals 60 days ago, we would have done sub-optimal deals. And so what we wanted to do is we want to take care of the immediate cash needs and we've done that. And now we're going to roll out a comprehensive plan with all of our stakeholders and kind of, hey, we're going to build it up. As Abhi builds the schedule back up, you'll get paid accordingly. And we're all in this together, right? We're all -- we all want Azul to be successful. And so we're going to do that. We're going to work very closely with them and they're our partners.

Q - Josh Milberg {BIO 19336060 <GO>}

Okay. That's very helpful color. John and Alex. And talking about the interest of keeping you guys healthy, the government probably has that interest too. And so I was just

wondering if you could also touch on the status of the BNDES funding. Obviously, there's been a lot of different reports out there, but one thing that seems to be the case is that the BNDES may be contemplating a lower amount of funding that it had previously and that they are, in fact, insisting on a private market participation.

A - John Peter Rodgerson {BIO 17734009 <GO>}

Hey Josh --

Q - Josh Milberg {BIO 19336060 <GO>}

I don't know if you can address that, yes.

A - John Peter Rodgerson {BIO 17734009 <GO>}

Josh, I think the country is in a tough spot right now right? And so I think that maybe what was previously announced and what they're able to do is going to be different. But I will tell you that, one of our largest stakeholders is the Brazilian government. We paid BRL2.5 billion last year in taxes, right? And so a healthy Azul is very important to Brazil.

When you talk about how many cities we serve, our importance to Embraer, our importance kind of across the board. And the reality is they don't have as much money as they previously thought, right? And I think they would love to kind of help fund the industries like you're seeing elsewhere in the world in the U.S. and in Europe and other places, but I don't know that they have that. I think it's disappointing that the dollar amount is lower.

But I think that, what it brings a lot of clarity to us as to what we need to do. And so I think it's going to make the conversations with all of our stakeholders a lot easier. Hey, we're going to get this back. We had one of the best airlines in the world. We're going to be back there. Everybody is going to get paid in full. Let's just move forward.

I think the good thing about the BNDES deal is it's just equal, right? And so what I get is what Gol gets, what LATAM gets. And so there is nobody kind of getting a preferential treatment one way or the other. Nobody's negotiating a better deal or worse deal. And so look, any money is being -- anybody is welcome right now, obviously, because it helps us across the board. But again, I think we're disappointed that it's not bigger. I think it would -- but we will do what we need to do to have a strong airline over the next 18 months. And certainly, we'll do everything we need to do to have a strong airline 10-20 years from now.

Q - Josh Milberg {BIO 19336060 <GO>}

Okay. Much appreciated.

Operator

Our next question comes from Matthew Wisniewski with Barclays. Matthew, your line is open. Matthew, your line is open, you may proceed.

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Q - Matthew Wisniewski {BIO 21239168 <GO>}

Hi. Sorry about that. Thanks for taking my questions. (Technical Difficulty) for cash burn (inaudible)

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Sorry, Matt, we can't hear you at all. Sorry, Matt, you're breaking up. Maybe we'll go to the next question, and we'll come back to you, Matt, if we can fix your line.

Operator

Our next question comes from Mike Linenberg, Deutsche Bank.

Q - Michael Linenberg {BIO 1504009 <GO>}

Yes. Hey. Good morning everybody. A couple here. So you've been able to work out a deal with Embraer and to push those airplanes back a few years. Where are you with respect to Airbus? I know you mentioned that you were in talks with them as well as the engine manufacturers on the airplane. How many neos where you expect it to take maybe this year, next year? And what is the right number? Or does it seem like no airplanes for the next few years is the right number?

A - John Peter Rodgerson {BIO 17734009 <GO>}

Mike, obviously, no airlines for the next few years is the right number. I think getting Embraer done and being Brazil's largest domestic carrier in terms of destinations and being how important we are to Embraer is a clear signal that we want to send to Airbus. It's a negotiation, right? And so we have to negotiate. I think, all OEMs want to deliver aircraft and no airline in the world wants aircraft and so it's an active negotiation.

But we wanted to set the example with Embraer and use that in our discussions. We're talking about deferrals. We're not talking about cancellations. And I think as -- depending on how the conversation goes, it could get to cancellations. I think it's in Airbus's best interest to try to keep the portfolio alive and make sure that Azul is healthy, so that we'll be able to take the full complement of their aircraft over time.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Yes. And the big aircraft number that was coming, Mike, were Embraer. So if you remember, we were kind of halfway done with our fleet transformation and we already have over 40 neos. So the next couple of years we're going to be primarily replacing E1s with E2s. So on the Airbus side, we're talking about low-single digits. It's not -- it's nothing as relevant as what we had on the Embraer side. But, we also believe -- and we're pretty close to an agreement with Airbus as well. So you can essentially consider that we will not take aircraft that we don't need.

Q - Michael Linenberg {BIO 1504009 <GO>}

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Okay. No, that's helpful. And then maybe just a question to Abhi. It was interesting to see that you are ramping up a little bit, May versus April. We know in the U.S., it seems like that the low point was mid-April. Our sense was that Latin America was maybe a month, maybe six weeks behind the U.S. so sort of maybe it's a two-part question. One, have you seen the bottom? Or did you -- as you cut and LATAM cut and Gol cut, did you realize that opportunistically and because of your fleet and the fact that like you mentioned you fly all the way down to, I guess, ATRs and caravans now with the Two Flex acquisition, were there markets there that you realized you could serve? And like you said that they would cover the variable costs that it made sense? And so that the additional service is less a function of demand improving and just you being more opportunistic? I'm just really curious about the ramp back up. And I realize it is modest, but it's noticeable.

A - Abhi Manoj Shah {BIO 18968426 <GO>}

Yes. Hey Mike, thanks. Yes. So in terms of the bottom, I think that we are well off the bottoms, which is good news. I would say the bottom in terms of demand was in second and -- second week of April, second and third week of April. And we have seen a bounce back from that, which is very good. The size of the bounce is sort of commensurate with how we've been ramping up the demand, the network. So we're kind of going pace-to-pace with what we're seeing in terms of demand. And so that is good news.

In terms of how we are deploying the fleet, as David said, it's flexibility. So we are flying today caravans in markets. We used to fly with ATRs before. We have ATRs flying in the north, for example, in cities like Belem, which we supply Embraers. And we have Embraers flying 80, 20 routes, for example. So we definitely are using, I would say, two really, really powerful tools to bring back the network. And the first is flexibility, smaller aircraft feed bigger aircraft. We're using our multiple hub structure, obviously, Campinas, Belo Horizonte and Recife. And we're recreating the hub structure that we had, and we're driving a lot of connectivity.

If you remember, Azul was always a very connected airline and now that's even more important. Corporate demand is not back yet, especially big corporate demand, which tends to be more local. And so it's really connecting demand that's driving the bulk of the revenue right now. And 90 of our 100 daily flights on average are in Campinas, Confins or Belo Horizonte or Recife. Of the 59 routes that we're flying, only four of them have airport-to-airport competition and not even on a daily basis. And so it's very much the Azul network flying very much within our hub structure where we are strong. And that's allowing us to ramp up, because we have the aircraft that we can use to access demand and we see how it goes.

We actually had one route, believe it or not, that we started with caravans, went to ATR, now flying A321 up in the north, actually. And so -- and what we've been able to do is, thanks to our crew members, our pilots and flight attendants, we have the ability to roll a schedule on a weekly basis including crew schedules. So we are planning revenue, system operations and crew scheduling. Upgrading, downgrading aircraft by week, launching a new cruise schedule every single week and that allows us to take opportunities in the network. So we're launching new routes actually by week to see what works. We're removing some stuff that doesn't work. So that's sort of how we're thinking about it.

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Obviously, unit revenue is important. We have to be able to generate variable cash. That's really important. And we have to be able to contribute to the network, which we already have. The flexibility together with the connectivity is really important and that's allowed us to bring back the network. And we'll keep doing this. We're discussing this week and early next week. We'll start rolling out early part of June. One thing that's really helping also -- it's helping and makes things little bit more difficult is demand is actually very close-in, right?

There are a lot of Brazilians right now that are looking for the second half of the year. And so even if you have a flight, a new route or a new flight out to sale out two to three weeks, that's like more than enough time right now. And so that's sort of giving us opportunities to put flights pretty close in to see what works. So it's kind of all these combinations that allowed us to bring back to about 118 flights a day on peak days where we are now and we're currently in the process of evaluating early part of June.

A - John Peter Rodgerson {BIO 17734009 <GO>}

And Mike, we've also done a lot of kind of charter flights to repatriate Brazilian. So we actually had -- A330 was in Rome yesterday picking up Brazilians. We flew to Lima. We have flights going to China to pickup medical equipment. So we're trying to utilize our fleet as much as we can in that way as well.

A - Abhi Manoj Shah {BIO 18968426 <GO>}

Yes. And also just to ad, we dedicated two A320 aircraft. We've adapted two A320 aircraft for all cargo operations with the boxes on the seats. Of course, we have ATR quick change. We have our two freighters. So we have almost nine aircraft sort of dedicated to the cargo team, and they are making hay while the sun shines, which is also good.

Q - Michael Linenberg {BIO 1504009 <GO>}

Yes. No, thanks. That's a fantastic answer. And I don't think there's any airline in the world that probably has the ability to do crew bids on a weekly basis. So that does speak to the flexibility. Just one quick last one and this is probably to John and Alex. So the burn now is BRL3 million to BRL4 million per day. And I think at the end of the day, whether we get to the fourth quarter and revenue is down 80% or down 30%, obviously, we're hoping for the latter. The fact is, I'm sure that you have to get to breakeven no matter what the backdrop is.

And my sense is that it's a come hell or high water situation for you. Where at what point - can you just walk us through the trajectory of the BRL3 million to BRL4 million now? And where do you think you are third quarter, fourth quarter, maybe early '21? Do you -- do we get to that cash breakeven? Is it the fixed cost basis tied to the fleet and the fact that you do have a sizable number of aircraft leased? Does that -- does it make it more difficult to get to that breakeven? How are you thinking about the trajectory or at least the pace of the trajectory? And thanks for my questions.

A - John Peter Rodgerson {BIO 17734009 <GO>}

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Mike, I'll start and then I'll pass it over to Alex. We will do whatever it takes, okay? It's that simple, right? And we will do whatever it takes. We're owners of this company. We built it from scratch. We will do whatever it takes to get Azul to the other side of this. We have several stakeholders that will do whatever it takes as well, because they are long-term partners of Azul, okay?

So they've been extremely flexible on payment terms as of right now. And we need to get back to a more healthy economy where we're flying the majority of our fleet. But we will do whatever it takes. And so our Chairman is one of the most optimistic guys I know right, but we're having an earnings call telling you we're planning for 40% flight schedule in December, okay? And so that means that pushing out all these E2s. It shows a conservative approach by management.

It's not appropriate to be taking new metal when we're asking for our current partners to step up and help us, right? So that was a big signal as well to our current partners. It's like, look, we're not going to bring new metal in unless you're getting paid 100 cents on the dollar, right? And so that's one of the big signals that we wanted to bring to all of our partners.

I'll let Alex kind of talk through the specific on the cash part.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Yes, Mike, you're right. I mean, it's going to be easier for us to get to breakeven as the demand comes back. But it's also a question of the variables that we are working with, right? So depending on demand but also depending on our cash position, depending on our cash sources, right? How is the negotiation with the BNDES evolving? What other sources

-- the world is not going to be un-financeable forever. There is going to be a point where - and even now you're seeing some airlines tapping the capital markets. And there will be a point where we will be able to tap the capital markets, where we will be interested in accepting the terms that the market is looking for. And so all of those external variables are going to determine what we're going to do and that's how, as John put it, we're going to do whatever it takes.

And so what we're doing here is we're preparing all these different scenarios, right? And obviously kind of preparing for the worst. And preparing for the worst means that, even if demand doesn't come back, the cash outflow is going to reduce as required, right? And we'll make sure that the franchise is alive and well for when the recovery starts. So the development or the evolution of this cash flow will very much depend on what the outside variables will look like. And we have a strategy for each one of those sort of scenarios that we're looking at. And some of these are, like you said, easier to execute and more friendly. And we're looking forward to those scenarios and hoping we're going down those roads. But if we're going down the road of more delayed recovery and we'll adjust accordingly.

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A - John Peter Rodgerson {BIO 17734009 <GO>}

And Mike, just back to what I was saying earlier, lessors, banks, crew members, everybody depends on Azul, airports, right? The Brazilian government. And so all these people are going to say, "Hey, let's get through this, right? I mean this is not -- this was not a mismanagement of a business that led us to where we are today. This is something completely out of our control. It's out of Brazil's control and so we're going to have to get through it. And so it makes the decisions a lot easier and a lot clearer when you take a conservative approach and say, "Hey, this is what we're going to do." And we're all united.

I mean this management team has been together for 12 years, right? And so we know each other. We know what we're capable of. And it's -- we're back to old Azulville, right? It's a small airline again. And we're going to build it right back up. And so we're excited to build it back up. We talked about, hey, when we put these lights back on, we're going to do it differently this way. We're going to be more efficient this time. We're going to make sure we do things better. So we're going to build this back up.

And you -- what Alex has kind of continued to say is, we have an unbelievably great franchise. Nobody flies to where we fly to. Nobody has a product that we have. Nobody has the crew members we have. Nobody has the partners we have. That's the greatest asset of all.

We have the best business in the world. And we're going to come back from this. It sucks right now. It sucks for all of us right now. It sucks for every single person on this call right now, but we're going to come back, right? And we're going to come back, because we're going to do everything we have to do to come back. And so this is an unbelievable great franchise that was built and we're proud of it and we're going to see it through.

Q - Michael Linenberg {BIO 1504009 <GO>}

Very good. Now thanks for taking the time. Appreciate it, everyone.

Operator

Our next question comes from Pablo Monsivais, Barclays.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Pablo? I think we're having kind of trouble with Barclays' line here.

Operator

Pablo, your line is open.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Yes Pablo -- for Matthew and Pablo, maybe we'll call you out later.

Q - Pablo Monsivais {BIO 17389900 <GO>}

Hello?

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Pablo, are you there? No. Yes let's go to --

Q - Pablo Monsivais {BIO 17389900 <GO>}

Can you hear me?

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Yes. Yes, go ahead, Pablo.

Q - Pablo Monsivais {BIO 17389900 <GO>}

Okay. Perfect. One question I have is, if you guys can help me to reconcile your amortization schedule. I think you that have short-term debt for BRL4 billion. However, when I see your amortization table for the next quarters, it's only BRL6 million. So it is correct to think that you have like BRL3.5 million amortization obligation in the first quarter of 2021?

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Yes. No, that's an easy one, Pablo. As of March 31, we have a facility with OPIC on engine maintenance financing. That as of March 31 -- it's the only covenant that we have that is measured on a quarterly basis. So as of March 31, the -- we had breached the covenant, but we've received the waiver already. So for balance sheet purposes, we have to put it in short term. But for practical purposes, because we already have the waiver and we have the waiver actually until the end of the year in advance already, it's not really a short-term debt anymore.

Q - Pablo Monsivais {BIO 17389900 <GO>}

Okay. That's great. And regarding leveraging your receivables, I remember that in the conversations we have had, you already have BRL1 billion of that in. I'm not sure if that BRL1 billion is already in the first quarter numbers. Do have any aim from that?

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

No. So the ability to leverage receivables is something that's related to the credit markets, right? So it's something we believe we will be able to tap into over time. But it's not something that we're looking at right now. What we're doing is advancing receivables, right? That is still ongoing. It's still functioning. So again, for those on the line that maybe are not familiar with the Brazilian market, we in and all -- the businesses here in Brazil sell a lot in installments and credit card installments. And you can either pull those installments forward and get cash today, which is what we're doing, or you can let that balance be used as a partial collateral for debt, right? We've done that in the past. We will be able to do that in the future. But right now we're just advancing the receivables.

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Q - Pablo Monsivais {BIO 17389900 <GO>}

Okay. Great. And one last question, if I may. On your cash burn ratio, what is the estimate of lease payments right now?

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

As of right now today, it's zero. But as we go forward, it will ramp up according to the demand environment and our operation.

A - John Peter Rodgerson {BIO 17734009 <GO>}

Flight schedule. As the flight schedule steps up, it steps up.

Q - Pablo Monsivais {BIO 17389900 <GO>}

Okay. Great. Makes sense. Thank you very much.

A - John Peter Rodgerson {BIO 17734009 <GO>}

Thank you.

Operator

Our next question comes from Stephen Trent, Citi.

Q - Stephen Trent {BIO 5581382 <GO>}

Hi, good morning everybody and thanks very much for taking my questions. Just a few quick ones for me. One, I saw you guys provided some very helpful detail on the hedge positions. And I guess you've kind of a piece of the fuel hedges for this year. Could you tell me more or less sort of on a net-on-net what percentage you now have covered for this year? Just in case I misread it. Thank you.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Sure. So based on the conservative schedule that we assume, we're roughly -- we're a little below 50% hedged for this demand, right? Obviously, if the demand kind of changes, that number changes. But what's important, Steve, is that we should not expect any big cash outflows from these hedges, right? We've been negotiating with our banks. And we've made some payments in March -- especially in March. But over time, whatever payments we need to make will not impact our short-term cash position. We will be either rolling those contracts forward or we will be rolling over the payment, the settlement of these hedges.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Very helpful. Alex. And just another quick one. I think this might be for Abhi. Abhi, what you -- very helpful detail in terms of the connecting traffic has kind of driven the bounce, not corporate demand, but non-corporate demand. When do you guys think

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about the cadence of potential recovery, is it fair to say that some modicum of corporate demand has to a trend before Azul might start to think about testing higher fares?

A - Abhi Manoj Shah {BIO 18968426 <GO>}

Yes, hey, Stephen, yes, I mean look, absolutely, corporate demand is a big part of all demand in Brazil, especially the big companies like Vale, Petrobras, the banks, they are some of the biggest consumers of air travel in Brazil. So one thing that's held corporate travel back is Sao Paulo is still under quarantine, right, which has been extended until May 31. And we'll have to see kind of how the numbers are and what kind of that recovery looks like. Sao Paulo is obviously the biggest consumer of air travel in Brazil and so that drives a lot of demand across the entire domestic network in Brazil.

So yes, corporate is going to be very, very important and it's something that we're watching very carefully to measure how we bring back the network. Our commercial teams are continuously talking to our corporate customers, our travel agency partners and we are seeing some signs like, for example, is bringing back about 30% of their production and things like that. But we haven't really seen any big signs yet from the banks for example, that they're bringing back a corporate travel in a big way. The banks are a big sign, Vale and things like that.

So I think we have to wait for a little bit of Sao Paulo demand coming back, the Sao Paulo state, the interior of Campinas region before we make broader steps in terms of the network, But, obviously, we're evaluating everything we can. We're trying to find pockets of demand. I would say, right now the oil and gas sector is probably over achieving in terms of who's flying and the financial sector is probably under-achieving in terms of what's flying. And that's what we'll watch for over the next couple of weeks.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. That's really helpful. I will leave it there. Thanks, Abhi, and I hope all you guys are good and healthy. Take care.

A - John Peter Rodgerson {BIO 17734009 <GO>}

Thank you.

Operator

Our next question comes from Florence Majartis[ph], MetLife.

Q - Analyst

Hi. Thanks for taking my question and thanks for your time. Just a couple of questions. The first one is regarding the financial covenants. I saw in the financial statement of 2019 that you have two covenants, one is regarding to the local vendors and other one regarding to aircraft financing. The second one is measured quarterly. I would like to double check if you are already asking some waiver, because leverage already picked up to 5 times and

the leverage -- the covenant is at 5.5 times. This is the first one. And the second one is regarding to the cash burn, if it includes the principal payments. Thank you.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Yes. So on the covenant side, the one that's measured quarterly as you mentioned, is the one that we mentioned to Pablo that we already received a waiver, not only for Q1 but also Q2, Q3 and Q4. For the other one, it's the same counterpart that has both the debenture and the aircraft financing. So it's really just one discussion. It's kind of two facilities. But one discussion with one counterpart,

it's measured annually. We are already in discussions and we have full confidence that we'll be able to get a waiver. We've gotten a waiver from this counterpart in the past, back in the Brazilian recession 2015 or 2016. They're great partners of ours. So we're very confident that we will get a waiver on that, but it's only measured at the end of the year.

On the cash burn, like we mentioned, there are no significant debt repayments this year. The main one that we haven't rolled over yet is also the debenture that expires only in December. So the cash burn includes interest. It does not include principal, but we don't expect there will be a cash outflow related to that principal. And in Q2, which is the BRL3 million to BRL4 million cash burn that we mentioned, there is no principal payment.

Q - Analyst

Okay. Thank you. Very clear, very helpful. Thanks Alex.

Operator

Our next question comes from Victor Mizusaki, Bradesco BBI.

Q - Victor Mizusaki {BIO 4087162 <GO>}

Hi. I have two questions. The first one, we have seen a lot of discussions about the city configuration given the COVID-19. So I'd like to know if you already had any kind of discussion with the Brazilian government in order to mitigate this kind of risk. And the second question, let me take a look on your numbers. We can see sublease receivables going up in the first quarter. So just to double check, if this is related just to FX or for example, TAP is not paying.

A - Abhi Manoj Shah {BIO 18968426 <GO>}

Hey, Victor, Abhi here. I'll take the first one regarding the seat configuration. One thing I think the industry is doing very well is communicating a lot with the customer on safety on board, right, regarding cleanliness, masks, all those kinds of things. There has been no discussion and there has been no request for discussion regarding seat configuration.

We don't believe it's on the agenda for the Brazilian industry. Nobody has raised it. Nobody's asked about it. And I think the industry by itself is doing a very good job of communicating, that it's safe on board in terms of air quality in terms of friendliness, using

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masks, all those kinds of things. Pretty much all the airlines are doing similar things. And I think we need to continue this, so that we all make the customer feel confident when they fly. I think it's in everybody's best interest to do so.

We are not planning any changes in seat configurations. We do not have any limitations on seat configurations right now. We are flying 118 flights today with customers onboard. And all this time, I don't have any reports of customers wanting to get off the plane, because they don't want to sit where they are, of customers not being confident or customers not comfortable regarding the flying experience. So I think the airlines are doing a good job of communicating. I think we've got to keep doing this, but we have no plans or are in no discussions about changing anything in regards to seat configuration.

A - John Peter Rodgerson {BIO 17734009 <GO>}

I would just add to that as well. We've got over 13,700 crew members. And to date, we have 25 cases of COVID in our entire company. And only one of them was hospitalized. And so we have a very young population, a very healthy population that travels. And so we've taken great care. We're measuring the temperature. Everybody's wearing masks. And so I think we're really looking very closely to ensure that our crew members and our customers are safe when they travel.

One -- your question, reference to TAP, it's a standstill for everybody with respect to lessors, right? And so we're not paying lessors in the second quarter. So there is no reason for TAP to pay as well, right? We're kind of united in that. They're our partner. They've halted flying for the time being to preserve cash. And so it's simply that. And so their obligations remain the same, but we've kind of across the board have done a standstill. And so that's all that you're seeing there.

Q - Victor Mizusaki {BIO 4087162 <GO>}

Okay. Thank you.

Operator

Our next question comes from Zina Mytilinaiou, William Blair.

Q - Anezina Mytilinaiou {BIO 21037640 <GO>}

Yes. Thanks for taking my question. Just a confirmation on the amount of the BNDES deal. So the recent headlines took about BRL4 billion. This amount refers to all three companies or only to you and Gol? And do you have a very specific deadline to go operate? Or there is a flexibility around that? Thank you.

A - John Peter Rodgerson {BIO 17734009 <GO>}

So we haven't decided yet on -- we have a call today with them to understand better the structure, what it means. They've set aside BRL4 billion. They said, it's for one to three carriers, right? And so I think that, that's the total amount. If it's divided by three, obviously,

it's less. If it's two airlines take if it's more. And so -- but we're working through that, right? We need to understand it. It's kind of a different structure than what we're used to.

And -- but we're -- we have several questions with them, and we need to make sure that if we were to potentially take that, and we haven't decided yet, whether it gives us the flexibility we need to rebuild the airline the way we believe it should be rebuilt. And so we're working through that. And I think what will most likely happen is most airlines will get to the next step with them. And this is still something that's quite about 45 days away from any funding. And so kind of getting to the next stage is probably important, but that's the only thing that we have to say about it right now. We'll give you further clarity on it as we move forward.

Operator

Our next question comes from Savi Syth, Raymond James.

Q - Savanthi Syth {BIO 17476219 <GO>}

Hey. Thanks for the follow-up. Just a clarification on the cash burn and just generally on revenue, what you're seeing in the commentary previously was very helpful. Just wondering if -- as you're kind of selling these flights, what level of revenue you're seeing and if that's mostly kind of people using up vouchers? Or are you actually getting kind of cash in? And what level is assumed in that kind of cash burn figure?

A - Abhi Manoj Shah {BIO 18968426 <GO>}

Yes, Savi, yes. So actually, it is cash in. I would say, the vast, vast majority is cash in. We do obviously are -- have travel credits out there. But I would say that customers really haven't decided yet when and how to use those travel credits. So we're tracking this every day. And the vast, vast majority of the money coming in is new cash in. And one thing -- and I'm looking at with regards to these flights is not just sort of the revenue on the flight does that cover the variable cost.

But more importantly, does the new cash in cover the cash going out in terms of the operations of these flights. And that really is even more important right now to make sure that the new real cash coming in, whether it's credit, whether it's debit, whether it's cash, net of vouchers, net of travel credits is able to cover the variable cost. And even with netting out sort of those types of forms of payment. The new cash in coming in itself is able to cover the variable cost of these operations. And that is our goal going forward, to maintain it that way.

Q - Savanthi Syth {BIO 17476219 <GO>}

That makes a lot of sense. Thank you.

Operator

Our next question comes from Mike Linenberg, Deutsche Bank.

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Q - Michael Linenberg {BIO 1504009 <GO>}

Yes. Hey, thanks. Just a quick follow-up here. I know just early in the call, I think, John, you had mentioned that TudoAzul is a potential source of liquidity. I know you've tapped it in the past for sort of the advanced mileage sale. What would be -- what do you think is the potential capacity there and maybe even sense of timing? Is that a 2020 type event? Any color on that would be great. Thanks.

A - Alexandre Wagner Malfitani {BIO 2519089 <GO>}

Sure, Mike. So TudoAzul brings in, on average, about BRL1 billion a year from outside the Azul system, right? So not including the points sold to the airlines. So real cash brought in from banks and from retailers and from customers themselves, right? Because that's a big part of TudoAzul's business.

We have the Club, which is a monthly subscription plan, which is actually very resilient in this situation. We still have a lot of members paying monthly their dues in the TudoAzul Club, and that's great cash coming in the door. So that's up to BRL2 billion. If we could structure it like, let's say, in a very friendly environment, right? I think you could have as much as BRL2 billion to pull forward from two years, right? I think partners would be comfortable with that, and there are ways to kind of structure. Obviously, in this environment, we're not talking about anything in this magnitude.

I think today, we are in current negotiations to actually bring in as much as BRL200 million, those are kind of term sheets that are being exchanged right now. But as the situation improves, I think that's what people are willing to advance, given the situation that we are today, how much we're flying. And also on their side, how much their customers are using credit cards, right? That affects sort of the demand for points.

But as we recover, everything benefits, right, everything improves because people will use their credit card more. They will get more points. They also get more comfortable on their own economic situation. And also, we will have more flights to offer to them, which also helps, right? So I think we're sort of in the bottom. I think that today, we could get at least a couple of hundred million. I think this could increase as the situation improves.

Q - Michael Linenberg {BIO 1504009 <GO>}

Very helpful. Thanks, Alex.

Operator

(Operator Instructions) Ladies and gentlemen, this concludes today's question-and-answer session. I would like to invite John to proceed with his closing statements. Please go ahead, sir.

A - John Peter Rodgerson {BIO 17734009 <GO>}

I'd like to thank all of you for joining us today. We're working hard. We're going to get through this, especially with our great crew members on our side, our great partners. And

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so if you have any individual questions, feel free to follow-up with Andrea or Alex, myself or Abhi. We appreciate everybody taking the time. Stay safe.

Operator

Ladies and gentlemen, that does conclude the Azul's audio conference for today. Thank you very much for your participation, and have a good day.

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