

Q1 2012 Earnings Call

Company Participants

- Andre Gaia, Empresa Brasileira de Aeronautica S.A.
- Frederico Curado, Empresa Brasileira de Aeronautica S.A.

Other Participants

- Alexander Anson, Analyst
- Cai von Rumohr, Analyst
- Joe Nadol, Analyst
- Milan Posarac, Analyst
- Myles Walton, Analyst
- Nicolai Sebrell, Analyst
- Noah Poponak, Analyst
- Ray Neidl, Analyst
- Stephen Trent, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. and welcome to the audio conference that will review Embraer's First Quarter 2012 Results. Thank you for standing by. At this time all participants are in a listen-only mode. Later we will conduct a question and answer session and instructions to participate will be given at that time. If you should require assistance during the call, please press the star key followed by zero. As a reminder, this conference is being recorded and webcasted at ri.embraer.com.vr.

This conference call includes forward-looking statements or statements about events or circumstances, which have not occurred. Embraer has based these forward-looking statements largely on its current expectations and projections about future events and financial trends affecting the business and its future financial performance. These forward-looking statements are subject to risks and uncertainties and assumptions including among other things general economic, political and business conditions in Brazil and in other markets where the Company is present.

The words believes, may, will, estimate, continue, anticipate, intend, expect, and similar words are intended to identify forward-looking statements. Embraer undertakes no obligation to update publicly or advise any forward-looking statements because of new information, future events, or other factors. In light of these risks and uncertainties, the forward-looking events and circumstances discussed on this conference call might not

occur. The Company's actual results could differ substantially from those anticipated in the forward-looking statements.

Participating on today's conference call are Mr. Frederico Curado, President and CEO; Mr. Andre Gaia, Head of IR; and Mr. Rodrigo Rosa, Controller.

I would like now to turn the conference over to Mr. Frederico Curado. Please go ahead, sir.

Frederico Curado {BIO 2004589 <GO>}

Good morning, everyone, from a very rainy and dark Sao Paulo. So a few words about the quarter; we delivered 21 E-Jets and we also sold 12 new aircraft, ten for Azul, one for BA and one for Japan Airlines. With those orders we have a total of 1,063 aircraft sold in the E-Jets family. This comprises 60 companies in 42 countries so the customers keep expanding.

Last two additions as operators are Bulgaria Air and Estonian Air, which are important to the (capitalarity) and the liquidity of our assets of our aircraft.

As far as the Executive jets, we had 13 deliveries this quarter. Of those 12 were Phenoms and one Legacy. Importantly, we keep developing the Legacy 500 in every test we can before a flight for these initial tests, which shall happen the Third Quarter so we are on time for that so low tax, low speed taxi, high speed taxi and also GVT, ground vibrations tests, all going well so far.

As far as deliveries with those 13 deliveries in the quarter we reached 300 Phenoms delivery to the market for the worldwide market and we have also gotten to the mark of the 100th business jets, Embraer business jets in Brazil. Those are important marks for us.

Here in business jets our bigger customer, Minsheng in China, which has an important legacy 650 order also ordered the Lineage 1000 so we announced three aircraft recently for the same customer, which validates the strength of the Chinese market and in particular Embraer growing presence in that market.

We obviously continue to invest in our global support network. As the fleet grows, we continue to invest in spare parts, new service centers and according to the plan.

Shifting gears to the defense and security, we -- this business is growing as predicted. It's showing robustness in its growth so in this quarter it grew 20% of the revenues of the Company. Our outlook for the year is 16% so it's probably going to stay between 16% and 20% throughout the year. This is our expectation.

We had the first flight of the second AEW 145 for India Aircraft of the three so the program is it's moving.

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We also announced during the FIDAE Air Show three new customers for the Super Tucano, all of them in Africa. And also I think important to emphasize, we acquired the participation that the ADS had in OGMA so our stake in OGMA and Portugal now is 65%, the remaining 35% in the hands of the Portuguese government.

Now, so a bit about financials; we had a slight reduction in our backlog and our revenues we reached \$1.16 billion, two-thirds of that coming from the commercial aircraft business, 20% defense and 13% business jets.

(inaudible) margin is more or less where we thought it should be, 23%, showing a consistent behavior as far as the last few quarters. With that we also -- which is an operating margin of 7.4%, which is \$86 million vis-à-vis the 1.15 revenues.

Our SG&A it's (inaudible). Our SG&A we broke the trend, which was throughout last year a growth was increasing cost in SG&A so we were able to reduce both in Reals and in US dollars and this is clearly a focus for us not to allow it to keep growing but rather stable or being more and more efficient as we go.

So with the \$86 million of EBIT our EBITDA was \$148 million, 12.8% on sales and we remain solid about the outlooks of both EBIT and EBITDA, for revenues, EBIT and EBITDA for the year.

Net income of 5.4%, \$63 million, is coming from a large impairment of last quarter but again relatively in line with our expectations.

On the cash side a little bit of a frustration of revenues, which of course as we lost some - a few deliveries, which we shall deliver in the next quarter. These penalize our cash flow a little bit. You can see that reflected in the increasing inventories but again, volatility among quarters so nothing that should not be resolved within the course of the year.

And to finalize, we took some low-cost short-term indebtedness also to cope with this little bit of the frustration in some revenues in the quarter. We remain very solid in cash position. We remain very comfortable as far as the maturity and the cost of our indebtedness.

So our net cash in the quarter, I mean at the end of the quarter, was to \$300 million, which is roughly \$2.3 billion in cash, about \$2 billion in debt, with that difference gives us the \$300 million in free, in net cash, net cash/debt.

So with that, I am open for Q and A and thank you for your attention.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from (Rava Bandata) of Royal Bank of Canada. Our next question comes from Noah Poponak of Goldman Sachs.

Q - Noah Poponak {BIO 16071528 <GO>}

Fred, I wondered if you could talk about what happened with your CFO. It seemed a little odd to see him come on and leave in that short of period of time and what the plan is for the next person in the position.

A - Frederico Curado {BIO 2004589 <GO>}

No he got a -- from a (inaudible) got an un-refusable proposal. That's the best way to put it. He got a -- as you may remind, he came from Usiminas and had his whole career -- I mean, not his whole career but a long time career there as lately CFO. Then he left the company, went to another steel mill company, came to Embraer and he was invited -- he's taken office I believe today or maybe yesterday it was. Yesterday he took office as a Chairman of Usiminas and I understand in a very, very attractive and aggressive package, so markets. There's absolutely nothing, mom and pop market aggressiveness in Brazil. It's a good place to be the CFO in Brazil by the way now, Noah.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay and plans for a replacement?

A - Frederico Curado {BIO 2004589 <GO>}

Yes weeks, we are weeks away from announcing our new CFO and we will be certainly somebody really very seasoned and with experience in both Brazil and the U.S. markets so it's final stage of our search.

Q - Noah Poponak {BIO 16071528 <GO>}

Great. On commercial orders they've been relatively light year-to-date. Could you just elaborate a little bit more on why that's been the case and I guess more importantly, what your expectation is for the remainder of 2012 for commercial orders?

A - Frederico Curado {BIO 2004589 <GO>}

We -- there is -- Noah, there is some softness in the market clearly, not to the point that gives us let's say a major concern. We still see China with strong prospects. Asia is kind of resilient. Europe obviously is very soft but option activity is small, ones, ones and twos here and there. We, by the way, just had just one airplane for BA. That's no large deals coming from there. Some slowdown in Latin America, although it's still some growth. I think the Azul story in Brazil relatively speaking is a good story so we just had another 10 airplanes for Azul.

I think we can be a little bit more optimistic about the U.S. and so overall we are at this stage we are sticking to our feel that it is feasible that we maintain a one-to-one book-to-bill ratio and let's see how the U.S. market unfolds. Of course the U.S. there activity tends

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to be large but so we are cautiously optimistic. We are kind of -- we have a stable, I think a reasonable view of what's going to happen throughout the year.

Q - Noah Poponak {BIO 16071528 <GO>}

Do you now need one of the larger binary U.S. scope clause driven orders to have book-to-bill of one in 2012 or can you get to that one times level without any of those larger one-time U.S. orders?

A - Frederico Curado {BIO 2004589 <GO>}

It is tough to answer. Let me put it this way. At this stage I would not say that and if there is such a certain, a large order like that, I mean we are going -- let me answer you in a different way. If we have one of those large orders it certainly is going to pass. We are going to take those beyond the one-to-one. So we have not given up yet ex US as far as our ability to keep up with this might growing or I mean (inaudible) is no concern and we are sustaining orders, the revenues in our guidance but if you expand your request for the next three years, maybe.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay great. Then last one for me, the tax cut benefit from this Brazil stimulus package clearly positively impacts you. Can you talk about the degree to which that does or does not help you in the year 2012? Then can you quantify what the annualized impact is whenever it's going to be the case that it impacts you for a full year?

A - Frederico Curado {BIO 2004589 <GO>}

We do have some positive impact this year, though I don't think it's going to be let's say huge. Things from announcement to implementation takes a while in this country. There's a lot of regulation and the way that things happen so between expectation announcement and real I'd say accounting of those results there is not only delay but sometimes there is some (heat) lost in the system. On a stable I can't answer you let's say for next year. If everything remains the same as announced, probably it's like \$100 million tailwinds.

This year will be something between zero and less than that, certainly much less than that because you know, some of the measures will not impact our costs until the second half and some not even until the last quarter. So it's in the next two months we'll have a more clear picture but let's keep in mind that those things are there to try to offset some of the handling that we have so, which I mean it's we are working very hard, as you know, to keep our efficiency and productivity and competitiveness.

So this is -- I think this is old to us. It's not something which is -- it's really like a gift so it helps a lot. You know, last year, as you know, 10% increase in pay rate, it's difficult to keep going like that so it's refreshing that there is some concern and awareness in the Brazilian government that the Brazilian industry needs some more level playing field in whatever form which is possible.

Q - Noah Poponak {BIO 16071528 <GO>}

Got it. Thank you, very helpful. Thanks a lot.

Operator

Cai von Rumohr, Cowen and Company.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Yes thank you very much. Fred, if you could update us on the tone of bus jet demand and kind of your thoughts about anything you might do if Hawker or parts of Hawker become available?

A - Frederico Curado {BIO 2004589 <GO>}

Well bus jets we are seeing some; we're taking more calls in the United States now so we have to hope. As you say, if this were a hope and belief but we're hoping that there is some recent activity. We are busier in that respect so I think -- again, I think we are at this stage just keeping to our guidances.

As far as Hawker, we are following up the situation. We are evaluating how this thing is going to unfold. Obviously their financial situation is difficult. We -- maybe some assets could be of interest of Embraer. We just have to see how that develops but there is a possibility that some assets become available pre or post bankruptcy, we will certainly take a serious look in how that could leverage our ramp up of our own executive jet business.

For example, the infrastructure of support, that's something we keep investing so the purpose is for synergy there and at the product line we have to see whether there is some synergies which could be complemented. But this would be let's say our view. It's not a target in itself. It's something which may or may not become an interesting opportunity.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Okay and going back to Noah's question on the stimulus, could you give us a little more specific kind of -- it's obviously very small this year but maybe some help in terms of the rollout as we go through the year in terms of selling and G&A expense? You've kind of still told us we're doing R&D about \$100 million but should we just continue the rate of selling in G&A in absolute sense or do they tend to trend up as they did last year?

A - Frederico Curado {BIO 2004589 <GO>}

No definitely not, Cai. We have to contain and we are -- this is bringing us -- calling our attention. I mean last year we had a step function in our SG&A. Some of it is good. Some of it reflects increasing commercial activity as we're investing, for example, more flight demonstrators and we are trying to stir up more sales.

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On the overhead side it has to be, as it has been a holy war, against overhead costs so I think this slight reduction of the less for in this quarter shows a trend. I mean it is in worst case scenario has to be a flat number, worst case scenario, and that's something we're going to keep combating very fiercely inside the Company.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Okay if you just take -- you mentioned as we get to 2013 that we should be about \$100 million from the stimulus and yet if you kind of take the formula that 14% of COGS is Real based and most is research and 80% of G&A and so on and you apply the 16%/17%, you come up with a number on paper of \$200 million. Is that the better number or is it a smaller number because you reinvest some of it? How should we think about that?

A - Frederico Curado {BIO 2004589 <GO>}

I'm going to ask for the support of Andre here.

A - Andre Gaia

Cai, I think the numbers you are inferring refers to the total labor costs and the benefit of 20% goes over just a bit, the payroll itself, so you have to take this number divided by 1.8 approximately and then apply the 20% benefit. So then you get closer to this \$100 million that Fred mentioned.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Okay very good and on your question on SG&A, just so I am clear, does that mean we should be looking at about a rate of close to \$180 million the next couple of quarters, in that ballpark?

A - Frederico Curado {BIO 2004589 <GO>}

I think that's a fair assumption.

Q - Cai von Rumohr {BIO 1504358 <GO>}

Okay terrific. Thank you very much.

Operator

Ray Neidl, Maxim Group.

Q - Ray Neidl {BIO 14015874 <GO>}

Basically I was just trying to clarify this, the negative impact on the earnings this year. It looks like it was more financial and it related to the tax deductibility of the dividends and the exchange rate but also on top of that you kind of alluded to it, the administrative expenses up. It looked like salary cost was up due to the -- partly maybe due to the Real. Is that pretty much a summary of what's happening there, the basic operational results sort of look solid but it looks like it's more financial matters and the dividends have really negatively impacted the income for this quarter.

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A - Frederico Curado {BIO 2004589 <GO>}

There is always some volatility in the mix of (inaudible) and price so this element was always there and in First Quarter of last year was exceptionally positive. We emphasized that many times last year but yes we had this -- the non-distribution of interest on capital reduced our ability to get more favorable income tax and, as far as the RBG adjustment, it's a normal process as we do every quarter. We had new appraisers or new appraiser. I'm not sure one or two. Whatever, it's still they appraised -- the appraiser base that we use with our auditors to keep track of the -- with values of our fleet, there were some changes here which reflected this. I think it was \$17 million or--

A - Andre Gaia

\$11 million.

A - Frederico Curado {BIO 2004589 <GO>}

\$11 million, sorry, \$11 million of change and FX a little bit, I think about 2% is variation in the--

A - Andre Gaia

Varied 2.4.

A - Frederico Curado {BIO 2004589 <GO>}

So it's not in anything but it's a combination of two or three factors that -- but again I think it was a relatively as expected quarter except for the little miss about maybe the \$100 million in revenue therefore impacting the cash generation and inventories. And that for no large surprises here.

Q - Ray Neidl {BIO 14015874 <GO>}

Okay but you don't feel that the administrative costs are getting out of hand, something--?

A - Frederico Curado {BIO 2004589 <GO>}

No not at all and, as I said, we -- this \$180 million we think this could be used as a trend to going forward.

Q - Ray Neidl {BIO 14015874 <GO>}

Okay great and you said going forward there was some softness in the market worldwide. Were you just talking about the executive jet or are we talking about the commercial as well?

A - Frederico Curado {BIO 2004589 <GO>}

No when I say softness, well, the business there has been soft for some time so we are seeing some positive signs in the United States. When I said softness I was referring more to the airline side.

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Q - Ray Neidl {BIO 14015874 <GO>}

Okay great and finally the AMR write off we know there's a major restructuring going on at American Eagle right now and you're taking a penalty up front but to me when they get the new scope clause agreements in the bankruptcy there might be a huge opportunity for Embraer to sell them the 170s or 190s. Is that something that you're looking at? Is that a potential advantage that could happen maybe three or four quarters down the road?

A - Frederico Curado {BIO 2004589 <GO>}

We are actively involved in the new discussions with American between (American BNBS). We expect that that discussion, as to our understanding, it's going well. We believe this should be over. I mean this let's say the 145 fleet, the discussions should be over some time around the end of May. Then you have to see when is American going to emerge from bankruptcy. There is -- there are discussions about the future of American Eagle going after a larger aircraft depending basically on scope clauses.

We believe AMI will emerge stronger from the final bankruptcy so the timing on the new fleet, it's hard to predict. It will have a direct result of when they actually emerge from bankruptcy but it is being discussed. The airplane is -- the E-Jets are perfect to grow their needs but there are obviously several other considerations to be made. So we are very close to the issue and hopefully will be able to maintain our strong presence there.

Q - Ray Neidl {BIO 14015874 <GO>}

Great thank you.

Operator

Myles Walton, Deutsche Bank.

Q - Myles Walton {BIO 6802513 <GO>}

I was going to go back to the SG&A map for a second if I could, Fred. So if you can keep this run rate it would imply SG&A for the last three months of the year as a percent of sales is only around 11% and I know there's some headwind on R&D but it's actually not that much. It would point to your operating margin guidance of 8% to 8.5% having in the 100 basis points of upside potential. Can you give us what's the put on the other side of that that would kind of force it downward?

A - Frederico Curado {BIO 2004589 <GO>}

Maybe there may be some uncertainty on the -- of course depending on the higher revenues. We have a band for the revenues. Obviously the higher we get the better it is to dilute fixed costs. There is that we always have some unpredictable elements so just being 3.5 months in the year I think that's too premature to raise our estimate but that's not necessarily. I would say more uncertainty these days, Myles, is our let's say position as far as the how things will unfold, other than knowing that we're going to have something negative to offset potentially some upside that we may have coming from our contention of costs and also whatever it gets from the stimulus package.

Q - Myles Walton {BIO 6802513 <GO>}

Okay.

A - Frederico Curado {BIO 2004589 <GO>}

Maybe towards mid year we'll have a clearer or I'll have a clearer, more clear, answer to your question and we'll see where we are, what we can -- it's just still a little bit too early to change.

Q - Myles Walton {BIO 6802513 <GO>}

Okay no that's fair. It just is good to hear that SG&A could contain at this level. The other question is on the service related revenue, total for the Company, aviation services. I think the guidance had been looking for kind of a mid teens growth in this quarter. I think if you compile all the service businesses together it's about flat year-on-year. Is that where the revenue shortfall came or is that as expected and there's just easier comps and acceleration to the back half of the year?

A - Frederico Curado {BIO 2004589 <GO>}

We missed a few deliveries in the quarter so there is some carry over for the next quarters. I think it came more from the airplane side. I don't know, Andre, if there is any on the service side?

A - Andre Gaia

Yes, Myles, in terms of services, services there is some level for unpredictable in this process because there's some of the sales are spot sales so it's hard to be precise on a quarterly basis. We do see some expansion in services this year as the fleet continues to grow, as it continues to age and as we continue to market to this broader and, as you can see by the inventories for instance, in the spare tools you see certainly some growth on potential having strong results so all that together we make us believe that throughout the year there's a matter of (inaudible).

On a quarterly basis, as I said, because of the natural the way that the sales happen, hard to say.

Q - Myles Walton {BIO 6802513 <GO>}

Okay and then the last one for me is if you look to year end obviously a weak cash performance here in the quarter as you had to build the inventories, as you alluded to, where does the net cash position come out by year end? Do you claim that all back plus a little or just kind what's the outlook for net cash by year end?

A - Frederico Curado {BIO 2004589 <GO>}

Well we are certainly shooting for a net cash position, not to lose that position. We have this year a significant commitment as far as investments so we should be relatively stable as far as our cash position realizing our -- once we make a degree our revenues and cash

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generation we will be able to perform all of our investments and still remain a relatively stable cash position.

Q - Myles Walton {BIO 6802513 <GO>}

Okay great thanks.

Operator

Joe Nadol, JPMorgan.

Q - Joe Nadol {BIO 3056499 <GO>}

Let's go back to the business jet area. Fred, you had some cancelations in the quarter. Could you discuss the magnitude of those and what you're really seeing in that area?

A - Frederico Curado {BIO 2004589 <GO>}

We did, Joe. We -- and this is probably the largest single contributor to all degrees in our backlog. We had a customer in the Middle East, which had a large order. I don't have it by heart but it had Lineages and Legacies, maybe even Legacy 500, and that alone is a significant piece of the cancellations in the quarter so I think this was a non-recurring event that really caused some step function in fact there.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay and--

A - Frederico Curado {BIO 2004589 <GO>}

I'm sorry, just to add this too, I mean we were not alone so this same customer also had cancelations with other players. This of course I cannot mention but I mean the identity but it was not only Embraer was affected by that.

Q - Joe Nadol {BIO 3056499 <GO>}

Was it a customer that passed away?

A - Frederico Curado {BIO 2004589 <GO>}

No.

Q - Joe Nadol {BIO 3056499 <GO>}

Oh okay.

A - Frederico Curado {BIO 2004589 <GO>}

Yes, yes, well, as a business you mean right?

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Q - Joe Nadol {BIO 3056499 <GO>}

Yes. Okay so if we look at your other income were there liquidated damages in there that were significant?

A - Frederico Curado {BIO 2004589 <GO>}

Some was recognized this quarter and some we recognized next quarter. There was -- I think there was a settlement there. I don't know, Andre?

A - Andre Gaia

That's correct.

A - Frederico Curado {BIO 2004589 <GO>}

Exactly there right? Yes.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay you delivered one large cabin aircraft and I guess it was to Jackie Chan. How many - your guidance is 15 to 20. Do you still feel good about that number?

A - Frederico Curado {BIO 2004589 <GO>}

Yes we do.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay can you update us on how many of those are sold?

A - Frederico Curado {BIO 2004589 <GO>}

I sincerely don't know. I think, Joe, I think it's fair to say that we either have orders or LOIs. It's not all, most of it, so the last time I spoke specifically about this guideline, I mean I felt comfortable about the prospect of achieving our numbers.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay.

A - Frederico Curado {BIO 2004589 <GO>}

Maybe during the week you can call us and get more information but I just don't have the number here with me.

Q - Joe Nadol {BIO 3056499 <GO>}

No it's okay. Fred, the -- going over to the re-engining of the E-Jets, is there any update on your schedule there or which way you're going to go on some of the various outstanding issues? You previously said on the time frame that year end was your -- by

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year end is when you were going to announce it. Is that possible it might slip into next year at this point or are you still targeting by year end?

A - Frederico Curado {BIO 2004589 <GO>}

We're not really in a rush there. I would say it's more likely that we, as an announcement, a full announcement, more I think it's going to be next year. We may announce some important milestones this year eventually. Engine selection, it depends on the (inaudible) placement of the (inaudible) but I think as a full disclosure of what we -- what is the aircraft etcetera, all the conditions, I think it's more towards next year.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay and then finally, I hate to beat the drum again on the G&A issue but I just want to make sure that we and everyone else gets a very good sense of where you are. If you look at the last several years your profile in administrative cost has always been up sequentially and quite significantly throughout the year and so can you tell us specifically were there any unusual items in administrative costs in Q1? And if not, what's really driving this and what are you going to do to keep the total SG&A flat the rest of the year because that's not what's happened historically? What measures are you taking?

A - Frederico Curado {BIO 2004589 <GO>}

Joe, we -- if you take Second Quarter of last year, we have 109 S sales (picture) for last four quarters. Since then especially we're 109, 103, 114 and the 109 now. To take you know, SG&A, they were 64, 69, 70 to 71 so I mean we're not seeing this derailed trend of growth. keep in mind that's everything which is in Brazil we got a 10% raise last year and this will be some partially offset by whatever it gets in the stimulus packages and obviously all of our efforts but it is not out of control at all and it's just we manage the Company also if we have some growth this commercial activity is natural that we have, on the variable side at least, to have some increase. So this is my cut. I see it's something which was showing a slight increased trend and we are working to reverse. We had that a little bit lower SG&A this quarter than last quarter.

Q - Joe Nadol {BIO 3056499 <GO>}

Yes I am not saying it's out of control and let's exclude the selling expense because you're right, that -- a lot of selling expense is good. Just looking at the administrative year-on-year you went from 57 to 71. I understand the 10% increase but labor is a relatively smaller part of the administrative costs so there must be something else driving it and but you've answered a lot of questions on this so I guess at this point we'll just wait and see how it plays out the rest of the year. Thanks.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you, Joe. It's just if you allow me, labor actions is a reasonable portion of G&A, not small, and the real, the real step up happened last year. I mean it happened from the First Quarter to the second, Third Quarter. I don't remember though if we had any extraordinary event in the First Quarter of last year so year-over-year looks ugly but I think compared the last four quarters you see that if there was a shift, if there was a step up, it happened actually about a year ago and I here I don't remember on there what a year

what's caused this from 57 to 64 on the First Quarter to Second Quarter. But I take your point, Joe, and this is -- as I said, this is part of our holy war against overhead costs.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay thank you.

Operator

Nicolai Sebrell, Morgan Stanley.

Q - Nicolai Sebrell {BIO 7321622 <GO>}

Following up on the labor topic, I was wondering if you could talk a little bit more about that. You've realized efficiencies and margin gains over the past five years despite the weaker FX and obviously a lot of that was lower labor intensity, greater automation, etcetera and so I was assuming -- I mean, I was looking forward to next year, 2014, as commercial and executive aircraft production recover, or so we hope, to pre-crisis levels. How do you expect you're headcount to change? Do you see that you might be needing to add a lot of people or is it such that your continuous gains and efficiency etcetera might mean that headcount doesn't change by a lot? That's the first question.

Then the second question is, if you don't mind following up on the cash position, when you re-engine the E1-95, and I know you can't make official guidance and you don't talk about CapEx per se, but how might you finance the program? Do you foresee leveraging up somewhat or do you think cash flow will be sufficient to pay for the program or is there some other option? Thanks.

A - Frederico Curado {BIO 2004589 <GO>}

So on the first off on the first question, the strategy clearly -- the best way to gain productivity, best strategy, is to contain costs when you're in a growing mode so we had to make the adjustment of the size of the Company a few years ago when there was the crash in the market so we adjusted that and that I think was a very sad but necessary measure to preserve the health of the Company and that -- I can tell you this.

The headcount is going to grow as we grow certainly at the lower base than in our growth so our labor costs will growing. Hopefully they will grow but that will mean that they're going to grow top line but different slopes. I mean they are going to grow -- we're going to use any perspective of growth as a strategy to improve our productivity. This is absolutely clear in our Company.

As far as re-engines--

Q - Nicolai Sebrell {BIO 7321622 <GO>}

But how are you going to finance the hand?

A - Andre Gaia

Well I think there the--

(multiple speakers)

I mean we don't have a--

A - Frederico Curado {BIO 2004589 <GO>}

It's a combination.

A - Andre Gaia

I think the answer or one thing that we're going to do but it's going to be a combination of the cash flows that we generate. Eventually some of that's financing or and of course the partnerships are going to be established with the suppliers. Between that there and three main companies and of course there are other options that are more interest or more attractive we may consider too.

A - Frederico Curado {BIO 2004589 <GO>}

I think it's fair to say these days we are not looking at capital, right?

A - Andre Gaia

No.

Q - Nicolai Sebrell {BIO 7321622 <GO>}

Okay and that's part of the questions. Then the last follow-up if you don't mind, we've got the Farnborough Air Show coming up I guess in July, be here before you know it. You mentioned that you might make an announcement or discuss efficiency gains in the e-jet. Can you say anything about that or any other potential catalysts that might come along?

A - Frederico Curado {BIO 2004589 <GO>}

We are -- I mean I don't always -- as we finalize campaigns we have to announce them so we have some campaigns to announce in Farnborough. I really don't know. We had the engine enhancements on the e-jet campaign. That's what we are doing and we will keep improving the airplane before the new generation, which will not come before 2018, of which we will start talking a little bit more completely probably next year but in the interim we will keep improving business jets and maybe we may have some -- if we get something of more sizable matter, we may announce something in Farnborough but I think it's not something which is defined completely as we speak now.

Q - Nicolai Sebrell {BIO 7321622 <GO>}

Thank you very much.

Operator

(Operator Instructions) Milan Posarac, Scotiabank.

Q - Milan Posarac {BIO 21061140 <GO>}

Just filling in for Turan Quettawala today so I have a couple questions. First of all, I was wondering if you guys can comment a little bit on how regional jet pricing is these days. Presumably your major competitor is pricing very aggressively to build up backlog so I was wondering if you can add some color to what pricing environment you're seeing out there.

A - Frederico Curado {BIO 2004589 <GO>}

Well I think the increasing rates of production of narrow body aircraft absolutely puts pricing pressure on the whole industry, not only for the two major players but for everybody else. I must -- I haven't seen anything really material up to now as far as impacting our discussion sales, certainly not what is already contracted. But I would agree with you that with the volume of production being put in the market has been depressing relatively new used narrow body aircraft and you see lead rates on secondhand relatively new narrow body aircraft, which I think may indirectly cause a pricing pressure in the whole industry. So in a very broad analysis this is what I see.

Midterm, no direct impact yet but I think long term we -- the whole industry may have a negative impact.

Q - Milan Posarac {BIO 21061140 <GO>}

Okay great thank you. And I have another question about some of the -- from the defense and security side would be the contracts in the works with the Brazilian border monitoring projects, wondering if you have any sort of update on the sense of the timing on that in the Brazilian government, what you're seeing on that?

A - Frederico Curado {BIO 2004589 <GO>}

I do. The RSB for this Sisfron, which is the surveillance system on the borders, it shall be released soon and with that we'll have a more concrete understanding of the timing and the steps and so forth but the start of the procurement of this system is imminent. We're probably going to see that very soon, the RSB, and from there we'll be able to have a better understanding of timing and volume of that so it is moving.

Q - Milan Posarac {BIO 21061140 <GO>}

Okay thank you and just one more question, if you could discuss a little bit about the recent I guess agreement or relationship you established with Boeing and just provide a little bit of context on that, a little bit of color, some more details and if you -- do you have anything to share with regards to that relationship?

A - Frederico Curado {BIO 2004589 <GO>}

FINAL

Well it's yes sure. It is an MOU of really principles and broad, I mean broad areas for cooperation. Relating to on one side technology in the aircraft I think the initial driver was safety in the cockpit but also efficiency in the cockpit, efficiency of flight all together. I could just go on one step back to say that Brazil and the U.S. have signed a cooperation agreement in civil aviation, which is really broad rules from air traffic control to open skies to collaboration at industrial level, so that's the umbrella.

So we -- both companies saw that there are some potential cross collaboration in research, also in lean manufacturing. Both companies are invest in lean manufacturing for several years now and what can come out of that is there is no real specific objectives or something we want to achieve. It's more like a path going forward, more like a framework of collaboration than anything else focused again on at this stage in R&D and in manufacturing, versus automation etcetera and let's see.

I think this thing will unfold and it will tell us whether or not some tangible results may emerge. It's the beginning of a journey so that's how we see it. And we see -- I'll just add that it's positive for us. Hopefully it's positive for Boeing also. It is certainly positive for us in the sense that it is a -- those are two companies which do not start doing things for the sake of just doing things and there is an interest in pursuing some opportunities together, which is I think is important.

Q - Milan Posarac {BIO 21061140 <GO>}

Okay. Well thanks so much for taking my questions today.

Operator

(Operator Instructions) Stephen Trent, Citi.

Q - Stephen Trent {BIO 5581382 <GO>}

Good morning, everybody, and thanks for the time, as always. Two questions from me if I may on the defense side; the first pertains to the KC-390 and forgive me if I missed your comment here but is everything on track for let's say pricing that product some time next year?

And my second question also pertains to defense. It seems that the momentum has received some tailwinds, so to speak, on the back of President Rouseff's visit to Washington. Can you generally say that over the past few months the number of potential KC-390 customers you're speaking to has either stayed the same or at least modestly increased? And if it has increased, can we say, for instance, that people are now far less focused on this foreign corrupt practices investigation that emerged in the Fourth Quarter? And sorry, that a bit long winded but if I could just get some color that would be great.

A - Frederico Curado {BIO 2004589 <GO>}

The KC-390 is on time. First flight is scheduled for 2014 and but there's certification and the end of the contracts 2016 if I am not wrong and I am (guessing) that I am right.

FINAL

Probably yes, probably some time around 2013 and it can't be much later than that, 2014. We should have discussions with the Brazilian Air Force about the serialization of this aircraft and if the airplane will be ready to start becoming a product in line by 2016, probably should have some price definition around '13/'14 so it's fundamentally on track.

All major suppliers are defined, engaged and no recurring development ongoing so this very -- as far as customers no, no -- we have no serious activity as far as adding new customers. I believe that the initial cluster of partners is there and probably has -- as the airplane comes to be more visible, closer to the flag as the airplane is actually physically visible and to your first point, we also have some more clarity on pricing, then I think the campaigns will start to happen.

Until then I think it's more like consultations or understandings what the airplane is and what can be etcetera. And I don't see any relation whatsoever between these let's say the closer ties between Brazilian aerospace and the (FTP) investigation by the SEC, which is (conducting) then to have its own course and I don't see any political play in that at all. It's just the technical investigation being conducted by independent law firm and we have just keeping patient to see what's the outcome of that.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay, Freddie, very helpful and thanks for the time.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you, Steve.

Operator

Alexander Anson, Santander.

Q - Alexander Anson

Good morning, everyone, and just a very few questions regarding FX rate; I would like to check whether you could disclose what is your assumption for FX rate that you have included in your guidance for 2012?

A - Andre Gaia

At the week we announced the guidance the FX rate was around 175, 172 and the base line we took for the guidance was around 170.

Q - Alexander Anson

Great thanks a lot.

Operator

(Operator Instructions) We have a follow-up question from Elan Boserak of Gusche Bank.

FINAL

Q - Milan Posarac {BIO 21061140 <GO>}

Thanks for taking one more. Just wanted to speak a little bit about Legacy orders and how order flow in general is going on that. There's a sense that they may be a little bit weaker and I don't know if you can share about some of the reasons behind that because it seems some of your competitors are seeing some improved order flow on this segment in the market so I don't know if there's any insight you could share on that would be great.

A - Frederico Curado {BIO 2004589 <GO>}

About the (Legacy 60)?

Q - Milan Posarac {BIO 21061140 <GO>}

Yes.

A - Frederico Curado {BIO 2004589 <GO>}

Yes well yes, I -- you know, we are I mentioned earlier that we have seen we have taken some more phone calls. The Phenom 300 is selling well, the (Legacy 60) not so much. We had delivered in our big year I think it was a little something between 36 and 40 aircraft if I am not wrong. I think it was 36 or 37 and the last year it was maybe a third of that, a little bit more than a third so yes I think there is room and the calls that we are taking and the activity that we are seeing improving are in the Legacy 650 so hopefully we will be able to have a little bit better performance on this aircraft. The 300 is selling well and the lower end to the 100 it's really I think the segment of the market that everybody is suffering the most, not only us but all the OEMs.

Q - Milan Posarac {BIO 21061140 <GO>}

Okay thank you so much.

Operator

(Operator Instructions) This concludes today's question and answer session. I would like to invite Mr. Frederico Curado to proceed with his closing statements. Please go ahead, sir.

A - Frederico Curado {BIO 2004589 <GO>}

Yes so thank everyone for the presence; I wish you a nice weekend and a good Labor Day. In Brazil Labor Day is next Tuesday so goodbye to you all. Thank you.

Operator

That does conclude Embraer's audio conference for today. Thank you very much for your participation. Have a good day.

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