

Q4 2014 Earnings Call

Company Participants

- Frederico F. Curado, President & Chief Executive Officer
- José Antônio de Almeida Filippo, Executive Vice President Finance and Investor Relations Embraer
- Luciano Froes, Head of Investor Relations

Other Participants

- Alexandre P. Falcao, Analyst
- Cai von Rumohr, Analyst
- Derek Spronck, Analyst
- Kevin M. Kaznica, Analyst
- Myles Alexander Walton, Analyst
- Noah Poponak, Analyst
- Turan Quettawala, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

At this time, the company will present its fourth quarter 2014 results. Afterwards, we will conduct a question-and-answer session and instructions to participate will be given at that time. As a reminder, this conference is being recorded and webcasted at ri.embraer.com.br.

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, 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, estimates, continues, anticipates, intends, expects and similar words are intended to identify forward-looking statements.

Embraer undertakes no obligation to update publicly or revise 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 may not occur. The company's actual results could differ substantially from those anticipated in the forward-looking statements.

Participants on today's conference call are Mr. Frederico Curado, President and CEO; Mr. José Filippa, Chief Financial Officer and IRO; Mr. Luciano Froes and Mr. Eduardo Couto, Director of Investor Relations.

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

José Antônio de Almeida Filippa

Okay. Good afternoon for the ones out here and good morning for the Americans who has joined us. We're going to go to our presentation of the conference call and the conference call for the fourth quarter and 2014 results.

But before I go into the presentation, I'd like to take this opportunity to share with you some important announcements internally here. We're happy to announce that, it's organization announcement which Luciano Froes that you know has been dealing with you for quite some time. I think three years now. He is assuming new responsibility in the company. He has taken over the position of Marketing Director for Executive Jet business. He is going to be moving to Florida. He is going to be based in Melbourne where we're developing our excellence center for Executive Jet business. And starting next week, Luciano will take up those – that responsibility. So we're very happy with that opportunity. It's a policy of the company to really try to give opportunity, especially for talents like Luciano. So we are very happy with that possibility.

At the same time, we are introducing Eduardo Couto, who is taking over the position of IR, new business development in mergers and acquisitions. Eduardo comes from Morgan Stanley. He used to be equity analyst so he knows the dynamics of the markets. So he knows the company. He knows probably some of you. So we have resolved to have these replacements, so we understand that will continue to a high level people dealing with the market representing Embraer.

So again, good luck, Luciano. Hope, of course, he will be available. We look and welcome Eduardo with it. So we are starting to take this big opportunity that we have these events as we can announce this and do this transition.

With that said, we start the presentation and go to page 3 for the ones that are remote. We get into 2014 in the fourth quarter highlights in terms of the corporate highlights. We have the celebration of the 45th anniversary of Embraer last October. We also remained committed with the sustainability and we are recognized by that with the fifth consecutive year in the Dow Jones Sustainability Index, as well we are part of the ISE in Brazilian Stock Exchange. In terms of management process and best practice, we were awarded by the National Brazilian Quality Award, which is the PNQ, very, very important recognition in the Brazilian industry presented by the National Quality Foundation, the FNQ. Also, finalizing this page, several other recognitions related to people management and ranked it as best place to work in Brazil and abroad.

Moving to next page, page 4, in terms of the commercial business highlights. First, in the fourth quarter, we have the delivery of 30 E-Jets in the last quarter, one of which was the

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E-Jet production number 1,100 was delivered to Aeromexico last year. In terms of sales activity, we have the order for SkyWest for seven E175, which represents actually an option conversion. And related to the E2 program development, we had the first metal cut of the E2 program, so we are in line with that development.

Next page, page 5 in still commercial business, now the highlights of the year, we had the delivery of 92 E-Jets in 2014. Also in terms of sales activity, we had 258 E-Jets sold in the year, concluding the only in the E2 590 commitments. This includes our orders, options and LOIs. And as a confirmation of the E-Jet program's success, at the end of 2014, we had over 1,500 orders with customer base of 65 airlines in 45 countries. And with that, we maintain our leadership in commercial jets in the segment of 70 to 130 seats.

The next page, moving on to Executive Jets business, in the fourth quarter, we had the delivery of 52 Executive Jets broken by 38 light and 14 large jets. In terms of sales, we have the conversion of 10 Phenom 300 options to firm order from NetJets. And also an important milestone in our Legacy 500 program, we delivered the first three aircraft in the end of the year.

The highlights of Executive Jets in next page for the year 2014, total delivery of 116 airplanes, 92 light and 24 large jets. Still in relation to the Legacy 500 program, we had achieved certification in Brazil, in the U.S., in Europe and Australia. Another important achievement in the Executive Jets business was that for the second consecutive year, the Phenom 300 was the most delivered executive jet in the market, 73 units. And as a result of our commitment to customer satisfaction, we are ranked as number one in AIN annual survey.

Moving to next page, page 8, the highlights for Defense and Security business. Fourth quarter, we signed the firm order for the first 28 KC-390 to the Brazilian Air Force. Regarding the Brazilian fighter program, we confirmed our participation with the signing of MoU with Saab for the development. And regarding the LAS program in the U.S., we remain on track and we delivered the first four aircraft to the U.S. Air Force.

Next page, page 9, still Defense and Security, for the year, reached annual revenues of \$1.5 billion, up more than 20% when compared to 2013. Also an important milestone of Embraer KC-390 program was the last month we had the first flight of the product. And regarding the programs in our controlled subsidiaries, we continue to advance on the SISFRON project through Savis. We had the important contracts for supply of radars and equipment through Brazilian government on Bradar.

The Brazilian satellite program was an important step which was the critical design review of the program. And finalizing the highlights on the defense, we signed a contract to supply new aircraft management systems for Brazilian and Indian government.

Okay. Next page, now returning to the overview of the financial results and we can move to page 11, starting with the backlog. We saw an important growth on our backlog throughout the year 2014 reaching in the end of the third quarter our all-time high level. In

the end of the year, we had almost \$21 billion in backlog which were broken by 65% on Commercial Aviation, 26% on Defense and Security and 9% in Executive Aviation.

Next page, in terms of aircraft deliveries, in Commercial Aviation in the left side, we delivered 92 aircraft in the lower end of the guidance range of which the great majority were the one 175 model. In terms of Executive Jet business, we surpassed our light jet guidance range with 92 deliveries, but had a reduction on the large jet deliveries with 24. We had a range of 25 to 30 in the large.

Next page, in terms of revenues, net revenues as a result of those deliveries in the revenues with Defense, we ended the year with almost \$6.3 billion in terms of revenues within the guidance range of \$6 billion to \$6.5 billion.

Next page, page 14, the breakdown of the revenues was consistent with our expectations. In the left side in terms of business, we saw a relative reduction in Commercial Aviation related to the growth of defense. Commercial Aviation was - from 2013 came from 53% to 50%, but we saw Defense growing from 19% to 23%, Executive Jet business almost remained the same in terms of 27% in the previous year to 26% now.

When we see these revenues broken by region on the right side, the highlights for the America markets especially because of the deliveries in the Commercial Aviation and the increase - the second participation of Brazil which was more related to the defense activities.

Next page, page 15, we see the same information now broken in a quarterly view. As we mentioned, we confirmed that we had a more balanced year. Remember that last year we had a concentration in the last quarter this year although we still see that the last quarter is the strongest, we saw more balanced revenues throughout the year. So we had like this \$6.3 billion and R\$14.9 billion in terms of net revenues.

Page 16, in terms of SG&A, our ongoing focus on the cost control reflects the reduction in the Argentinian (14:34) dollar and not only in dollar terms, but also in the percentage of revenues. We saw in 2014 a total of \$628 million compared to \$665 million in 2013 and the percentage of revenues coming down from 11% to 10% in 2014.

In terms of EBIT operating results, page 18. Here we show - before we go into the details of this chart, just call attention about the information that we have in 2013, you remember that we had this positive impact of the reverse of provisions from the American, as American recover from the Chapter 11 position and we've recovered provisions that we had, so we are taking that information out here to have the fair comparison. So, let me see there what we had in the year. We reached \$543 million in 2014, within the guidance range from \$540 million to \$620 million. But in terms of margin, we had 8.6%, a little bit lower than guidance range and the main drivers of that were basically coming from the lower end of the deliveries and also the higher than expected mix of the E-Jet deliveries in 175 concentration.

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The next page, page 19, information broken by quarter. You see that actually the fourth quarter of 2014 was below the previous year, even excluding the non-recurring effect. Again, basically, because of the mix in both Commercial and Executive Jets business.

Next page, EBITDA, page 20. We had a total of \$830 million with a 13.2% margin, within our guidance range for the year. What is the next page, the EBITDA broken by quarter, the same comments as the previous one, on a quarterly basis increased in the last quarter, but not as strong as we had in 2013.

The next page, the net income. We had a total of \$335 million of net income, and a margin of 5.3%. Just remember that this number is impacted by the deferred income tax which is impacted by the FX fluctuation.

Next page is net income broken by quarter, we see here that especially in the end in the last two quarters of the year, the lower amount was basically reflected by the effect that we have just mentioned, the deferred income tax because of the dollar increase against the real.

In page 24, the earnings per ADS and payout as a consequence of net (18:19) income, the earnings per ADS was \$1.82 and the payout was 27%, which complies with the Brazilian corporate law, and also reflects our pay - anticipation that we pay - will be paying every quarter.

Continuing to next page, inventories. We end the year with the total of \$2.4 billion, which was an increase compared to the previous year as we prepare for the 2015 deliveries. Going forward in terms of investment, we had a total of \$430 million in 2014, broken by \$47 million in research, \$230 million development and \$153 million in CapEx.

In terms of R&D, the depreciation of the real along with the good execution allowed us to end the year below our outlook. And as far as CapEx, we managed also our cash disbursement trying to avoid pressure on cash, so we end up with the \$430 million as we give outlook of \$650 million in the beginning of the year.

Going forward, next page, free cash flow, as we previously announced early this year and revised in our guidance, our cash flow was negative in \$404 million. As already indicated, the main drivers of this figure - the main driver actually was the high working capital requirements, mainly due to the accounts receivable increase, the inventories and also advances from customers. This was, of course, partially offset by the reduction in investments we just mentioned in the previous sheet.

Finalizing the results before getting to the outlook, our capital structure, debt profile remains in line with our business cycle needs. We have 5.4 years in terms of average terms and also only 4% of the debt maturing in the short-term in the next 12 months. In relation to net debt position, as a result of the negative free cash flow generation, we reported slight negative debt of \$85 million in the end of the year.

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Okay. That will conclude the financial results highlights and getting into the 2015 outlook. As we published in our earnings release, the outlook will be as follows. On page 30, the consolidated outlook, net revenues for the year from \$6.1 billion to \$6.6 billion, EBIT from \$490 million to \$560 million with margin from 8% to 8.5%, EBITDA from \$730 million to \$860 million with margin from 12% to 13%. In terms of free cash flow, we forecast that will be a use of no more than \$100 million. This number does not consider the recovery of accounts receivable impact that we experienced last year.

Going forward, next page, by business unit, in terms of Commercial Aviation, we forecast deliveries of between 95 to 100 E-Jets and net revenues from \$3.2 billion to \$3.4 billion. In the Executive Jet business, deliveries from 80 to 90 light jets and 35 to 40 large jets which will return to revenues in the range of \$1.7 billion to \$1.85 billion.

In terms of Defense, the guidance range for revenues between \$1.1 billion to \$1.25 billion and to balance the total consolidated we showed before, we had forecast \$100 million for other businesses revenues.

And last page, finalizing part of presentation, in terms of investment outlook, we forecast to invest \$650 million in 2015, broken by \$50 million in research, \$300 million in development and another \$300 million in CapEx. Primarily, those investments will be related to the E2 development program.

Okay. With that, we finished the presentation. So now, we open for questions.

Q&A

Operator

Thank you. And our first question comes from Cai von Rumohr from Cowen and Company. Your line is now open. Please go ahead.

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

Yes. Thank you very much, gentlemen. So your guide of 35 to 40 large jets, I think it's a little bit less than many of us were looking for, could you give us some color there in terms of what that assumes about Legacy 500 and 450s? How they are doing? And what that implies for your other larger biz jets? Thanks.

A - Frederico F. Curado {BIO 2004589 <GO>}

Yeah. Thank you, Cai. This is Fred. We - fundamentally, we are seeing a relatively stable Legacy 650 and Lineage - we have a background noise here, I don't know where - so Legacy 650 and Lineage 1000 relatively stable activity and the addition being Legacy 500. Probably, we will have couple of deliveries of Legacy 450. Can you guys hear some background noise or just me? Can you fix this, please? Cai, do you hear background noise or is it okay for you?

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

It's cutting in and out.

A - Frederico F. Curado {BIO 2004589 <GO>}

Okay. So the addition to our last year numbers, they are coming from the Legacy 500, and one could argue that we should be seeing larger numbers, larger numbers of Legacy 500s. So this is a - we really want to make sure that we have a smooth entry into service. We also have to acknowledge that the market is not booming since that we have a very strong backlog yet. But it is building up nicely and so the combination of market demand - yeah, it's much better now - market demands and assuring a smooth enter into service.

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

Okay. Thank you very much. And then, your margin in the fourth quarter looked a little bit lighter given the very strong volume that you displayed. Could you comment were there any negative adjustments? And secondly, maybe give us some color in terms of where the margins for each of the four - each of the business groups were and maybe some trend as we go into 2015?

A - José Antônio de Almeida Filippo

I think that in terms of the margin for the last quarter, we didn't have any specific adjustment that could impact, it was more related to the margins of each business and the lower end of the guidance range for the - and the mix like we mentioned in terms of the Commercial Aviation and also the mix in the Executive Jets [ph give the range] (27:55)

A - Luciano Froes {BIO 17907241 <GO>}

Yeah. And, Cai, giving a little more color - Luciano speaking here. The margins - gross margins for Commercial Aviation and Executive Jets were right around the range of 18.5%, 19%. And Defense and Security was closer to 10% and so for the quarter totals around 17.5%.

A - Frederico F. Curado {BIO 2004589 <GO>}

So talk about the adjustments, why was that so low, the adjustments for Defense.

A - Luciano Froes {BIO 17907241 <GO>}

Yeah. And it's important to mention that for Defense as we've explained in the past, it's best to look at an annual basis rather than a quarterly basis. There is a few factors that can influence that in terms of quarterly performance such as the phase in the programs in which we are, the composition of the revenue within that quarter from the various programs as well as potential FX variation. So, we can see, for example, in the first quarter of this year, as a reference, we had a bit of deviated effect as well to the upside. So looking on an annual basis, the margin came in pretty much as expected for the Defense and Security segment and higher year-on-year.

Q - Derek Spronck {BIO 17904184 <GO>}

Okay, hi. This is Derek, RBC Capital Markets. The CapEx or the free cash flow of guidance 2015, that doesn't include the recovery of the accounts receivable, is that correct?

A - José Antônio de Almeida Filippo

Correct. It does not.

Q - Derek Spronck {BIO 17904184 <GO>}

So technically, that could be a lot higher. How confident are you that you would recover this year the Brazilian accounts receivable?

A - Frederico F. Curado {BIO 2004589 <GO>}

You mean regarding this fiscal year or previous years?

Q - Derek Spronck {BIO 17904184 <GO>}

No, this fiscal...

A - Frederico F. Curado {BIO 2004589 <GO>}

Yeah.

Q - Derek Spronck {BIO 17904184 <GO>}

...2015.

A - Frederico F. Curado {BIO 2004589 <GO>}

Well, I think nobody in Brazil at this stage can say that we are comfortable with any receivables because, of course, the situation is public - of public knowledge. Having said that, the KC-390 is a priority program for Brazil. It's part of the pack which is that selected group of projects which have the highest priority in the government. And it is above all a real need for the Brazilian Air Force going forward. So, taking all that into account and also take into account that we are on-time and on budget, below receivables, we are on budget. So we are performing.

We have to believe that we are - will be one of the projects which probably will have has highest consideration as far as receivables. So, we are in discussions with the customer, in particular, the Brazilian Air Force to make sure that we do not incur into an increasing accounts receivable as we go forward. That may or may not result in a reschedule of the program, too early to tell. But we are not just blindly going forward, although, we are at this stage maintaining the rhythm of the programs.

Q - Derek Spronck {BIO 17904184 <GO>}

That's great. And one follow-on, from a CapEx perspective, are your new programs following relatively in line with your planned budget when you launched them, are they tracking ahead, better? And where do you see CapEx over the next few years trending?

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A - Frederico F. Curado {BIO 2004589 <GO>}

Okay so, that's primarily I'll split the answer in two. The P&D part of it, has a strong content in reals. So we are tracking that in dollars and we are relatively okay. I mean actually, we are a little bit below budget and we do have some tailwinds in that respect going forward. That's a question which I am going to anticipate the answer, probably some of you will ask, but we have referenced our planning and the basis for this outlook is FX of R\$2.8. So, there is - we do not know when the currency will stabilize, but, yeah, there may be some headwind there.

And in the most recent programs, in the Legacy 450 and Legacy 500, we are above budget because we have, and you may remember, delay in the program. So if you take the overall program since it launched in 2008 (32:48) there will be a little bit an overshoot in the budget. The E2 - 175 planes, the E175 was actually below budget and the E2 is a little bit better or lower than budget. So, I think the quality of our planning and control of cost is improving as we speak. And the 450, particularly, our 450, this is actually below budget as well.

The CapEx side, real talk about machines and tooling and to the hardware side which is mostly done in U.S. dollars. We are - I mean we are right there. The lower number that you saw in 2014 was much more a postponement of investments which did not impact the critical path of the programs, rather than better performance. But probably there will be some improvement there as far as a lower cost there, negotiations, et cetera. But that's mostly dollar denominated. So it's really a question of managing the cash flow, obviously, without impacting the critical path of the program. I hope I have answered it.

Q - Myles Alexander Walton {BIO 6802513 <GO>}

Thanks. Myles Walton, Deutsche Bank. I think Cai had asked about the margin trends into 2015 and I'm not sure I got the margin trends by segment into 2015, if you could do that. It does sound like you said 2.80 was your peg (34:20), so it seems like there is some margin opportunity on the upside there, if the current FX rates held. So could you just give a little detail by segments kind of what you're looking for, for margin trends, please?

A - José Antônio de Almeida Filippo

Yes, sure, sure, Myles. You didn't get because we didn't give them. Yes, so thank you for the gentle way of asking. But in this year 2015, probably you see a much more homogeneous margins, so in this band of 8% to 8.5%, the business will probably vary maybe plus or minus 0.5% to 1% each extra (35:00) of the band. So, as far as the gross margins, just to give you, it will be between 18.5% and 20%. So we are going to see margins. And as far as operating margins, there will be something 7.5% and 9%, so pretty much - or 8.5% and 9%. So it will be very homogeneous going forward, and that's how I see. And the other question was?

Q - Myles Alexander Walton {BIO 6802513 <GO>}

It just sounds like, number one, FX, where we spot it today would be a tailwind to your margin projection, if you said 2.80....

A - José Antônio de Almeida Filippo

If it stays at - so 2.90 is the headwind for defense business, but it is a tailwind for the other two businesses.

Q - Myles Alexander Walton {BIO 6802513 <GO>}

Okay.

A - José Antônio de Almeida Filippo

And it's a tailwind for the cash flow - mainly for the cash flow because all of our P&D which is very high. You don't see that in the P&L, but you do see that in the cash flow.

Q - Myles Alexander Walton {BIO 6802513 <GO>}

Then just one other one, as you look to the mix in Commercial Aviation, is this the worst of the mix? It looks like it's - maybe close to 80% 75 seaters this year, is this the peak of the worst?

A - Frederico F. Curado {BIO 2004589 <GO>}

Well, this is all relative because you have, of course, bigger aircraft tend to have higher prices, but not necessarily. So it's hard to say, it's worst. I think it's fair to comment that we did not - last year, Paulo mentioned a year ago in New York we were seeing a pressure on the pricing side and the mix, right, not only on the lower range (36:29) price but also in the competition of about 200 basis point, right, 2%. And so we are seeing a further pressure on pricing also and, of course, that's associated with the mix, it gives us a little bit more complicated outcome. That's why you saw a, call it, tepid margins for 2015. FX, and of course even stronger push on the cost sides, but there is that much we can do about cost. But that we will try it, of course, to recover that. But there is clearly a pressure on the top-line.

Q - Operator

So, here Joe Moore (37:24) from Merrill Lynch. I have two quick questions. First, still on the margin levels. I know that you said that you have to look on (37:29) an annual basis, but if you look specific to the segments this quarter, margins were very different from what we have seen in the previous nine months. If you could please give us some details on why was that? And second question on backlog, if you could elaborate on what growth what could we expect for 2015, it would be great? Thanks.

A - Luciano Froes {BIO 17907241 <GO>}

So as far as the quarter, I mean, the main drivers here, Commercial Aviation, certainly the mix, I mean, we saw especially compared with the fourth quarter of 2013, we saw higher concentration from the E175 model. So that was, I would say, one of the main drivers. And in Executive Jets, we did not deliver as many of the large aircraft as we did in the prior year as a comp. So, of course, the mix composition there again was a little bit of an effect. And for Defense and Security, obviously, it relates to the main programs that we have in the segment there. So program such as KC, or India, or some of the modernization

programs. But again, it's much more related to where we are in the stage of those programs than anything else, right?

A - Frederico F. Curado {BIO 2004589 <GO>}

And as far as backlog or sales outlook, we don't provide any guidance specifically about sales outlook going forward. We are looking forward - probably, we will achieve at least a one-to-one - book to bill ratio of one, probably higher than that in Commercial Aviation. So, Paulo has some activity going on which we hope to be successful not in the distant future. That offsets a little bit of that pricing, let's say, headwind that I mentioned a lot.

On business jets, definitely, we're trying to get a book to bill of at least one. We have to build up a stronger backlog in business aviation, so the industry is not very healthy enough, but as we have a better portfolio, we should and we work for, to assure at least a one-to-one book to bill ratio in the business aviation as well.

Defense, it will depend a lot on exports. I think the situation on the largest customer in defense which is the Brazilian government, and more frankly, more concerned about managing the accounts receivable and making sure that we have our ongoing programs on time and on track and being properly paced and there maybe new opportunities, yes, but that's I don't think - I think that's probably second in priority at this stage for the government and therefore for ourselves.

Exports maybe a nice surprise because we have now a second product to offer, not immediately, but longer term which is the KC-390, along with the Super Tucano, so having products in our portfolio, that helps. So we may have some nice surprises in exports.

Q - Turan Quettawala {BIO 6362141 <GO>}

Turan Quettawala from...

A - Frederico F. Curado {BIO 2004589 <GO>}

The reason for that, sorry, sorry, go ahead. Please.

Q - Turan Quettawala {BIO 6362141 <GO>}

Turan Quettawala from Scotia Bank. Fred, can you give us a bit of a sense on the biz jets side? What kind of pricing assumptions are you using? Are you expecting some pricing improvement in 2015 when you provide your guidance for the year? And also, do you have any write down (41:22) build up at the end of the year in 2014 here on the Legacy side?

A - Frederico F. Curado {BIO 2004589 <GO>}

Pricing-wise, Marco - when we close the call and then we have the presentation, Marco can elaborate a little bit more. Stability is a fair assumption, I think, stability - but we - I mean we are not seeing price relief as we expected. There is some - the used aircraft market is not getting worse, but it is not getting much better either, I mean get it for to

sell new aircraft. So there is strong competition out there and the demand is not that robust yet. So pricing is an issue going forward. I don't think it's going to deteriorate further. But Marco can elaborate a little bit more. And...

Q - Turan Quettawala {BIO 6362141 <GO>}

Are you getting any benefit from the Learjet at all or from the Lear...

A - Frederico F. Curado {BIO 2004589 <GO>}

Hard to say. I mean - well the Phenom is doing quite well as you saw and the 500s, I think my French, my style here. We have a beautiful case to show, but I think we have to market the aircraft better. It's - I had the chance to fly the aircraft yesterday personally and it is really a breakthrough. I don't think we are getting the message across as efficiently as we could and should.

Q - Turan Quettawala {BIO 6362141 <GO>}

And just lastly on the Whitetail inventory, is there any Whitetail inventory?

A - Frederico F. Curado {BIO 2004589 <GO>}

Maybe on the - maybe a handful, I don't know. I think (42:58). Yes, just - may be just a very small amount. On the Legacy side or on Phenom? I think Phenom 100, right? Yeah. Demo aircraft, so nothing material, I think. But Marco again can maybe give it better - a more precise answer.

Q - Turan Quettawala {BIO 6362141 <GO>}

That's perfect. Thank you.

Q - Noah Poponak {BIO 16071528 <GO>}

Hey, guys, it's Noah Poponak from Goldman. Fred, I just wanted to make sure I understood what you are saying about pricing in commercial jets going forward. I understood you to be saying, it should be an incremental headwind for a few more years because you will be layering in incrementally more airplanes that were - that came out of fairly difficult or aggressive competition? And then presumably you would need to potentially change price a little bit in the final years before you are bridging to E2. So that would all suggest pricing is an incremental headwind sort of the next three or four years, is that fair or is that inaccurate?

A - Frederico F. Curado {BIO 2004589 <GO>}

I apologize. I don't think I said that.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay.

A - Frederico F. Curado {BIO 2004589 <GO>}

So thank you for the question. The question is will it get worse, and I said it's hard to say, it got worse already. So this outlook already reflects a worsened environment. So we get worse than that. It's hard to imagine that we can get much worse than that. But we are working. We will be working on the cost side to brace for impact, whichever is the scenario. But personal opinion, today, I don't see getting worse. I don't. But we didn't see that coming either a year ago, so.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay. And can you talk about what margins - unit margins would look like in the first few years of E2 because typically a newer program can have lower margins for other reasons. But it also sounds like pricing is probably a lot better. So will margins will be better or worse or the same as you transition?

A - Frederico F. Curado {BIO 2004589 <GO>}

All we have at this stage is planned figures and there, they look good in the sense that reasonably good pricing for launch orders and nothing tells us that our recurring cost and our learning curve will be worse than what we predicted. So pretty much the same picture we saw before.

The program is going nicely. It's a little bit below budget. And I do attribute this harder pricing environment now to a combination of issues. Of course, as we get closer to the E2, now the E1 has become less and less attractive. And number two, the bulk of the demand is coming from the U.S. large orders. And number three, there are competition, very much starved for cash which gets the whole equation more complicated. So it's a combination of issues. I think Paulo is doing a really nice job in managing of volume and margins and then price and the margins. And again, cost variable, we - I mean, it's a relentless effort on our side. And you saw the SG&A coming down and that we can change, and of course, as well as the recurring - the COGS side of it to the extent that we can.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay. And then just one another one on the cash flow statement. Inventory was a source of cash, I think, for the second or third year in a row and you talked about that being because volume is going up, but volume is pretty flat across the business. Is there any way to do better on inventory going forward? And then can you also elaborate on why advances are a source of cash?

A - Frederico F. Curado {BIO 2004589 <GO>}

Okay. On - I mean, let's switch to get less boring just me speaking why not...

A - Luciano Froes {BIO 17907241 <GO>}

Yeah. Okay. In terms of inventory, inventory, I think, was more the picture on the end. I think in average terms, we'll not be seeing that. It's more like in the end of the year just to make the calculation that we had this year. So I don't expect - we don't expect to see inventories necessarily going down. But it's been a working capital requirement this year.

What we mentioned about the advance for cash, basically when you sell, we had an amount of cash related to the advance of customers that were not replaced by new sales, especially new Executive Jets business. So that's why it was the source of cash, but it reduced as we delivered, we compensated the advance, so we didn't generate the cash and we delivered, and it was not replaced by new sales.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay. Thank you.

A - Frederico F. Curado {BIO 2004589 <GO>}

And maybe as a suggestion, and take maybe one or a couple of more questions from the call. Then we can end the call and then turn back to the audience here. Yeah, one or two. I don't know how many people are in line.

A - Luciano Froes {BIO 17907241 <GO>}

No, no, no. They are from the call.

A - Frederico F. Curado {BIO 2004589 <GO>}

Yeah. There are four questions on the call, so let's take those four and close. Okay?
(48:34)

Operator

And your next question on the phone lines comes from Alexandre Falcão from HSBC. Your line is now open. Please go ahead.

Q - Alexandre P. Falcao {BIO 5515455 <GO>}

Thanks, guys. The line is really, really bad. So I'm not really sure that you actually answered this or not, so please forgive me if this is already answered. First, in what FX did you guys base your guidance for this year? That's the first question. And the second question is, can you run down on the defense programs, where you think - which are the ones that should not be impacted by any budgets cuts. What could be impacted, and I know that you're probably maintaining the same programs there. But if you could give us some granularity on what are the ones that are basically not going to be touched, and the ones that could be delayed would be perfect. Thank you.

A - Frederico F. Curado {BIO 2004589 <GO>}

Thank you, Alexandre. And I apologize for the poor connection. On FX, the reference of our planning outlook is R\$2.8 per dollar. And to your second question, we don't know. I mean, what do we expect is that the KC-390, which is, of course, the most important program of our portfolio, enjoys priority within the government. And it's part of the pack, it's a pack. So - but at this stage, we don't know. We are talking to customers and frankly, I don't think they know exactly how this whole thing will unfold, whole thing, by meaning the fiscal adjustment that the government is trying to perform.

So, I think we feel good about the quality - relative quality of our program vis-à-vis the other investments of the Brazilian government. But at this stage, we're maintaining our base in the program. But we are indeed in conversation with the Air Force to make sure that if there is a, let's say, affirmative trend to reduce the rhythm of the program, we have to adapt. And of course, we will. But that's premature at this stage to make any assumptions in that regard.

Q - Alexandre P. Falcao {BIO 5515455 <GO>}

Okay. And just a follow-up on that specifically on the KC. I'm assuming that you've already had your first flight. Development is basically done. We're talking about more or less, at least in our calculations, a neighborhood of around \$500 million that are needed to finish the project. And then you enter production. Is that really the case? Is this pretty much developed, or still you need something like that? And if there's a delay there, you're not going to be able to do your first delivery in 2016. Thank you.

A - Frederico F. Curado {BIO 2004589 <GO>}

Well, as far as what's left to invest, I can comment on the physical terms. We have the whole flight test campaign ahead of it, which is significant. I sincerely do not know and probably should take this question off line. About the \$500 million, I don't know. I sincerely don't know and we can address that offline later. But we had the flight test campaign, and most of the tooling is already there. But we're talking about something in the range of 2,000 hours, and that's a big deal and the second prototype, by the way also. So we are building the second prototype.

If there is a - the program is very, very tight. So we launched the program in 2008 and said we would fly this aircraft by the end of 2014 and we were like 40 days late. So very tight, and quite frankly, our performance has been amazingly on time. So there is no slack in planning. So if there is a delay, if there is a reduction in pace of developments, there's absolutely no way we can get the airplane certified by the end of 2016. So this is all part of the discussion.

Q - Alexandre P. Falcao {BIO 5515455 <GO>}

Fantastic. Thanks so much.

Operator

Thank you. And your next question comes from Kevin Kaznica from Citigroup. Your line is now open. Please go ahead.

Q - Kevin M. Kaznica {BIO 17875244 <GO>}

Hi, guys. Yeah, I'm also not really getting great quality on this side, a lot of cutting out. But I guess one of the questions that we'd have, does your 2015 margin guidance assume any payroll tax or integral (53:33) export help getting eliminated? Or somebody, I don't know if anybody addressed that yet.

FINAL

A - Frederico F. Curado {BIO 2004589 <GO>}

No. That's actually a new question for everybody and I think that's about \$20 million negative for us. Those latest changes which, as you may or may not know, Congress has sent back to the executive branch. So assuming it's going to be approved by Congress, that's going to be a minus \$20-ish million negative for us.

Q - Kevin M. Kaznica {BIO 17875244 <GO>}

Okay.

A - Frederico F. Curado {BIO 2004589 <GO>}

Sorry. And this is already incorporated in the guidance. So if it's not there, we should have a better \$20 million. It's a relatively low impact either way.

Q - Kevin M. Kaznica {BIO 17875244 <GO>}

Okay, very helpful. Very helpful. And also could you maybe talk a little bit about what happened on the Tianjin Airlines order that you announced in July for jets and why it hasn't been carried in the backlog yet?

A - Frederico F. Curado {BIO 2004589 <GO>}

We are still waiting fundamentally for the final approvals of the Chinese government. We had - Paulo may have more. Paulo, I think he is on the, how long have you got? Just a second. There is nothing I mean it's fundamentally waiting on the approvals or the customer is waiting on the final approval of the Chinese government.

Q - Kevin M. Kaznica {BIO 17875244 <GO>}

I'm sorry. You cut out.

A - Frederico F. Curado {BIO 2004589 <GO>}

No, there is nothing. It's fundamentally awaiting on the approvals of the customer. It's awaiting the final approvals of the Chinese government. There has been...

Q - Kevin M. Kaznica {BIO 17875244 <GO>}

There has been - go ahead.

A - Frederico F. Curado {BIO 2004589 <GO>}

There has been a recent state to state of Brazil to China discussion or forum and this item was on the agenda and the Brazilian officials got the assurance from the Chinese officials that they should not be concerned. The order will be confirmed this year. But we are fundamentally waiting. And of course, pushing the delivery dates as we wait. So we're not building Whitetails for Tianjin. But we are comfortable - confident that that's going to happen.

FINAL

Q - Kevin M. Kaznica {BIO 17875244 <GO>}

Okay. That's awesome. Very helpful. And then finally, can you elaborate on any potential order activity from any of the U.S. carriers this year, like SkyWest has a bunch of conditional orders, but only confirmed seven? Or like Alaska Air, do you see any others getting done? And what kind of activity do you see from Europe or Asia?

A - Frederico F. Curado {BIO 2004589 <GO>}

Yes. We expect to have something done for the U.S. We are engaged in a few campaigns and we are optimistic that we're going to capture some opportunities which are out there. Probably not in the distant future and there is also another order in Europe, which we are also optimistic that we can bag. So, Paulo has been very active. So we have at least - had several campaigns, of course, but more short-term. We feel better about this one in the U.S. and this one in Europe.

Q - Kevin M. Kaznica {BIO 17875244 <GO>}

Okay, great. Thank you very much. I'll let somebody else ask a question.

Operator

Thank you. And that does conclude today's Q&A session for today's conference. I'll turn the call back over to José Filippa for any further remark.

A - José Antônio de Almeida Filippa

Okay. So, thanks the ones that joined through the conference and so we are still available for the questions as we do through the IR team. Thank you.

Operator

Well, ladies and gentlemen, thank you for participating on today's conference. That does conclude Embraer's audio conference for today. Thank you very much for your participation. And have a good day.

A - José Antônio de Almeida Filippa

Thank you.

A - Frederico F. Curado {BIO 2004589 <GO>}

Okay.

A - José Antônio de Almeida Filippa

Let's continue here.

A - Frederico F. Curado {BIO 2004589 <GO>}

Back to the room.

Bloomberg Transcript

Q - Operator

I just want to make sure I understand the fourth quarter margin better. Going into the fourth quarter, you didn't change your margin guidance, did you just have - maybe a couple of 190s move to the right and maybe you've delivered 20 650s as you expected, is that kind of the fundamental dynamic or was there something else going on as you headed into the fourth quarter?

A - Frederico F. Curado {BIO 2004589 <GO>}

Yeah, we had that, yes.

Q - Operator

Okay, okay.

A - Frederico F. Curado {BIO 2004589 <GO>}

Yeah. To be more clear - I mean to be totally clear, we probably would have reached the bottom of our guidance in 2014, had we delivered a couple of airplanes which were not delivered and they are inventory and we do expect to deliver this year.

Q - Operator

Okay. And then on the KC-390 with all the flux, your defense guidance for next year, are you assuming in your guidance that KC-390 revenue is down for 2015?

A - Frederico F. Curado {BIO 2004589 <GO>}

No, we are assuming this budget that we are going to get paid for the 2015 budget. It does not assume anything from the - what is already in our accounts receivable. But it does assume that the full budget for 2015 would be paid. Yeah. So, if there is any reprogramming, there is a potential downside risk there.

Q - Operator

So on a pre-FX basis, is it - defense revenue should rise in 2015 but you get the pressure from FX year-over-year?

A - José Antônio de Almeida Filippo

In terms of revenues?

Q - Operator

Yeah, I am sorry.

A - Frederico F. Curado {BIO 2004589 <GO>}

Yeah. If you just take the last year which was close to \$1.5 billion, and you just bring the average FX that we had last year to \$2.8 billion, that number should be about \$1.25 billion which is the highest band of our guidance. Why? Obviously, showing a lower band of our

guidance because this year we are going to have probably two-thirds of the revenue in reals and one-third in dollars and last year was half and half. So there is a - so as far as activity, this was pretty much flat but fundamentally is the effect of the FX and the mix of Brazilian contract and U.S. contract - Brazilian denominated contracts and U.S. denominated contracts.

Q - Operator

Understood. Last question, Brazil wage inflation in 2015, is that incrementally worse or the same or...?

A - Frederico F. Curado {BIO 2004589 <GO>}

It's hard to tell inflation, does not look good. The Central Bank just raised the primary tax again, they referenced interest rates again. I think it's going to be very, very unlikely that's going to go above the devaluation of the currency. So we have probably kept, of course - so the value of the currency is probably going to be better for us any increase in wages at least in this year. Over time, it tends to catch up. But this year, probably, I don't see the U.S. dollar coming below 2.8 at all, and maybe higher.

Q - Operator

Thank you.

A - José Antônio de Almeida Filippo

Let's take one more question, please. Then we break for -nexts'ession.

A - Frederico F. Curado {BIO 2004589 <GO>}

And just remember that after this - after the presentation, we will be back and it will be for the whole afternoon. So we can always be available for further question. Any further question at this stage or should we - there is one. Sorry.

Q - Operator

I just want to ask on the Defense again. So you are not taking the \$300 million account receivable in your guidance, and you obviously said that there might be some risk to your overall revenue numbers. Can you give us a sense of what percent of the revenue is just coming from the KC-390 in 2015 on the D&S side?

A - Luciano Froes {BIO 17907241 <GO>}

This will be more clear in the presentation. I think you could have...

A - Frederico F. Curado {BIO 2004589 <GO>}

José, I think you can take that.

A - José Antônio de Almeida Filippo

Yeah.

Q - Operator

Okay. That's great. Thank you.

A - Frederico F. Curado {BIO 2004589 <GO>}

Should we take a break then?

A - Luciano Froes {BIO 17907241 <GO>}

Yeah. Just to confirm the schedule, can you put in the - on the...

A - Frederico F. Curado {BIO 2004589 <GO>}

Agenda.

A - Luciano Froes {BIO 17907241 <GO>}

Yeah, agenda. Okay. So what we have now as we will have a break, 15 minutes and then we get together back here to the presentation of the business units.

A - Frederico F. Curado {BIO 2004589 <GO>}

10 minutes.

A - Luciano Froes {BIO 17907241 <GO>}

Yeah.

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