

## Q1 2015 Earnings Call

### Company Participants

- Eduardo S. Couto, Director of Investor Relations, M&A and New Businesses
- Frederico F. Curado, President & Chief Executive Officer
- José Antônio de Almeida Filippo, Chief Financial Officer and IRO

### Other Participants

- Alexandre P. Falcao, Analyst
- Bruno Amorim, Analyst
- Cai von Rumohr, Analyst
- Derek Spronck, Analyst
- George Ferguson IV, Senior Analyst Aerospace/Defense & Airline Research at Bloomberg Industries, Consumer & Industrial Team Leader
- Kevin M. Kaznica, Analyst
- Kristine Tan Liwag, Analyst
- Myles Alexander Walton, Analyst
- Noah Poponak, Analyst
- Peter John Skibitski, Analyst
- Turan Quettawala, Analyst

## MANAGEMENT DISCUSSION SECTION

### Operator

Good morning, ladies and gentlemen, and welcome to the audio conference call that will review Embraer's First Quarter 2015 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. As a reminder, this conference is being recorded and webcasted at [ri.embraer.com.br](http://ri.embraer.com.br).

This conference call includes forward-looking statements or statements about the 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 believe, 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 statements and circumstances discussed on this conference call might not occur. The company's actual results could differ substantially from the anticipated in the forward-looking statements.

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

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

## **José Antônio de Almeida Filippo**

Okay. Thank you. Good morning, everybody, and thank you for joining Embraer first quarter 2015 results. As we usually do, we'll go through the presentation, and then we'll be ready for questions in the session.

So starting on page three, in the highlights of the business for the quarter, starting with the Commercial Aviation business, we had a delivery of 20 E-Jets in the first quarter of this year, and including in that number the first E175 related to the direct order of American Airlines out of the 60 in that order, and also - late delivery, sorry.

Now, in terms of orders, we had the KLM/Air France order for up to 34 E-Jets, including 17 firms and 17 options, which includes the current generation of the E-Jet 175 and E190. Also, continuing orders, the Republic Airways ordered additional five E175. As far as our customer base, we had the inclusion of KAL STAR Aviation, which became our first E-Jet operation in Indonesia. And finally, in relation to the E2 program, we received an important award, which was the Crystal Cabin Award related to our larger bin and individual seats in first class.

Now, in slide four, moving to Executive Aviation highlights, we had a delivery of 12 executive jets in the first quarter of this year, split by 10 light jets and two large. In relation to our Legacy 450 program, we continue to advance and we expect to enter into service in the fourth quarter of 2015. And related to the Legacy 500 programs, we had additional three important recognitions by the Aviation Week magazine, the National Aeronautic Association, and also Flying Magazine.

Moving to next page, Defense & Security highlights, starting with an important milestone of the KC-390 program, which was the first flight that happened early February this year. In terms of the LAS program development, we had the delivery of two aircraft in this quarter, and now five are already delivered.

Regarding Brazilian fighter program, we signed a partnership contract with Saab in the middle of this month. And in relation to our - the Brazilian satellite program, it was concluded the critical design review report this quarter.

Now, moving into the financial results, starting with page seven, firm order backlog reaching \$20.4 billion in the end of March, more than \$1 billion over the same period of last year.

Page eight, next page, in relation to deliveries, we had in Commercial Aviation the delivery of 20 E-Jets in the quarter. And regarding the executive jet business, we delivered 12 aircraft in the first quarter, broken by 10 light jets and two large jets. With that information, we are maintaining our guidance figure for the year in the range of 95 to 100 E-Jets and 35 to 40 executive large jets and 80 to 90 executive light jets.

Next page, page nine, revenues by segments. The total in the high-left chart, we had a total of almost \$1.1 billion of revenues in the first quarter. And when we break these revenues by business, moving to the right side, the Commercial Aviation business, a total of \$662 million in the first quarter; the executive jet business of \$167 million; and the Defense of \$213 million in the first quarter of this year.

In the next page, the consolidated figures. As we indicated, \$1.1 billion returned to almost R\$3.1 billion. But important here is that we have already mentioned that we are maintaining and confirming our 2015 revenue guidance between \$6.1 billion and \$6.6 billion.

Moving to next page, now, talking about SG&A expenses. We reported a total of \$129 million in the first quarter of this year, including \$43 million in G&A and \$86 million in selling expense. We remain focused on keeping those expenses under control and monitoring them.

Moving to next page, page 12, as far as operating results, we reported a total of \$80 million in the first quarter of 2015 with a 7.5% margin, in line with the margin of the first quarter of last year. We are maintaining our guidance for 2015 for the amount range of \$490 million to \$560 million and 8% to 8.5% margin.

Next page, page 13, in terms of EBITDA, we had a total of \$149 million in the first quarter, with a margin of 14.1%. Our outlook for the year remains unchanged, with a range of \$730 million to \$850 million and a margin of 12% to 13%.

On page 14, next page, regarding net income, actually net result, we reported a net loss of \$62 million in the first quarter, mainly due to the recognition of \$110 million of deferred income taxes. This already happened before when we have an appreciation of the dollar against the real. We had to do some considerations in terms of income tax, if the provision is not a cash impact; it's a deferred income tax. And that impacted our results in this quarter. Excluding this specific effect, we would have a gain of \$48 million in this quarter.

The next page, in terms of inventory, we end the quarter with a total of \$2.7 billion, an increase of \$291 million from the end of the year, reflecting the preparation of higher deliveries in the coming quarters.

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Next page, page 16, in terms of cash flow, we reported a negative cash flow of \$440 million in the first quarter of 2015, compared to a negative \$404 million in the same period of last year, confirming the seasonality of the business. But the main reason of this negative figure was the increase of inventories, as indicated before, coupled with a slightly higher accounts receivable primarily related to Defense & Security segment. Despite the cash consumption in the quarter, we are maintaining our outlook for 2015 of use of less than \$100 million in the year.

Next page, as far as investments, we had a total of \$106 million in the first quarter, broken by \$7 million in research, \$27 million in development, and \$72 million in CapEx. We are maintaining our indication of \$650 million as total investments for the year 2015.

Next page, page 18, finalizing the presentation before the Q&A session, our capital structure, we ended the quarter with a net debt figure of \$581 million, reflecting the cash consumption in the quarter. In relation to our debt, we remain with a comfortable profile, with an average terms of 5.3 years maturity and 85% portion in the long-term.

With that, we'll conclude this part of the call, which was the presentation, and now ready for the questions.

## Q&A

### Operator

Thank you. Our first question comes from Pete Skibitski of Drexel Hamilton. Your line is now open.

**Q - Peter John Skibitski** {BIO 6760095 <GO>}

Good morning, guys.

**A - José Antônio de Almeida Filippo**

Good morning.

**A - Eduardo S. Couto** {BIO 18009973 <GO>}

Good morning.

**Q - Peter John Skibitski** {BIO 6760095 <GO>}

I want to ask you, I'm guessing that you didn't collect on the large KC-390 receivable from last year during the quarter. Can you update us on your expectations for collecting that? And is there any contemplation to slowing the program down?

**A - José Antônio de Almeida Filippo**

Yes, Pete, actually this program goes as we expect it. As we indicated before, we are focused on maintaining and avoid to increase this accounts receivable. So that's basically

the pattern that we have for the first quarter. We had actually a little bit increase in the accounts receivable for the quarter, which was actually the snapshot of that in the end of March. But we received a portion, about \$50 million, in the beginning of April, which returned back to the level of the end of the year. So basically, that's the profile of that account.

**Q - Peter John Skibitski** {BIO 6760095 <GO>}

Okay. Understood. And just one follow-up. Can you give us a sense of how the segment operating margins trended in the first quarter?

**A - Eduardo S. Couto** {BIO 18009973 <GO>}

Yes, it's Eduardo, here. We have a consolidated operating margin of 7.5% in the first quarter. Commercial Aviation was around 12%; business jets, around 6%; and Defense & Security was around negative 9%.

**Q - Peter John Skibitski** {BIO 6760095 <GO>}

Okay. Just on that Defense, that's the lowest I recall for Defense in a while. Any particular one-timer impact that?

**A - José Antônio de Almeida Filippo**

Yes, Pete. Actually, the Defense as it has its revenues or its contracts they're more exposed to the real. We have to do an adjustment of FX base every quarter. We usually do this - we do this every quarter, but in this quarter, as we had an appreciation of the dollar, which is actually about 20%, that impacted negatively. But it's a non-recurring effect. It shouldn't be repeated going forward.

**Q - Peter John Skibitski** {BIO 6760095 <GO>}

Okay, great. Thank you so much.

**Operator**

Thank you. Our next question comes from the line of Turan Quettawala of Scotiabank. Your line is now open.

**Q - Turan Quettawala** {BIO 6362141 <GO>}

Yes, good morning. I guess maybe just a follow-on there, could you give us a sense of what that non-recurring item was, how big it was?

**A - José Antônio de Almeida Filippo**

What non-recurrent?

**Q - Turan Quettawala** {BIO 6362141 <GO>}

On the D&S business, you said there was an adjustment on FX that was non-recurring?

## A - José Antônio de Almeida Filippo

About \$30 million.

## Q - Turan Quettawala {BIO 6362141 <GO>}

Okay. That's helpful. Thank you very much. Okay. And I guess my next question, just when I look at the sort of the longer-term strategy of the company, I guess, if I look back two to three years, your Defense business was supposed to be, I guess, the growth leg here. E-Jets were kind of getting into a bit of a holding pattern. And obviously, that seems to have come true, here, with E-Jets kind of flattening out a little bit. But obviously, the Defense business is coming in a little bit weaker.

So my question, I guess, is, are there any other levers that you can pull here? The biz jet seems to be getting a little bit better, but certainly not as strong as maybe you would have liked. Or have the cards certainly been dealt and I think you kind of have to just make the best of the situation here? I'm just trying to figure out what kind of earnings levers you have over the next couple of years here?

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

Yes, this is Fred. Commercial aircraft, it's doing good. We have been able to sustain and actually increase quantity a little bit. Also have been able to so far to offset pricing pressures with efforts with lower costs and try to preserve margins as much as we can. So that's a sound business. Business jets, I mean, we had a particularly weak quarter. We missed a few deliveries. So that's why we are optimistic about increasing the numbers in next few quarters and meeting the guidance, as far as deliveries and revenues in that business. And again, that's also a growth engine for us, because we're still ramping up the Legacy 500 and we will have the Legacy 450 joining our portfolio at the end of the year. So there is growth in that segment for us.

In Defense, we have, of course, a strong dependence of the Brazil's armed forces. We have a lot of execution. We have a lot of contracts which assures us a very stable outlook for the next few years, most importantly the KC-390, of course. But that's a financial concern.

I mean, we have the payment problems. We have to believe that this will be solved soon. And we see Brazil in the next couple of years regaining traction, and that we continue to be positive in the long term for Brazil. And so as the Defense business is a long-term business, we are not really too much concerned about the long-term viability and growth potential of that business. As soon as we introduce the KC-390 in the markets, then we will have another product for exports. So that should be an add-on, a step function in that business, as well.

## Q - Turan Quettawala {BIO 6362141 <GO>}

Okay. Thank you, Fred, for that clarity. I guess, just one more question from my side. I know it's still early, but there's been a bunch of changes here at Bombardier. Just wondering if you've seen anything change from a competitive standpoint? I know there

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have been a lot of aggressive pricing there, in a lot of your markets there, from them. So just wondering if there's been any change there?

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

Well, they have been aggressive, very aggressive, for some time. So I would not have noticed, not personally, any significant change. I think it's - Alain is a capable guy, of course. And - but direct answer to your question, we did not see any specific change in that regard.

**Q - Turan Quettawala** {BIO 6362141 <GO>}

Great. Thank you very much.

**Operator**

Thank you. Our next question comes from the line of Cai von Rumohr of Cowen and Company. Your line is now open.

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

Yes. Thank you very much. So help me understand. Your gross margin was a spectacularly good 23.7%, despite a pretty lean mix. You didn't have any E190s, E195s. So you had all the lowest-margin commercial aircraft. So where do you expect gross margins to be for the year? And while I understand the revenues may be under some pressure, do you feel that your EBIT margin number maybe has some opportunity?

**A - José Antônio de Almeida Filippa**

Cai, thanks for the question. Yes. I think we had a situation in the first quarter, which shouldn't be the same for the rest of the year. I think that we had - if you think about the whole year, it should be back to the level of - as we indicated like level of the high two-digits - sorry, the high-teens, as we indicated before. But we shouldn't be the same situation of first quarter.

I think there is a combination of things here. If you take, like, executive jet business in this first quarter, we had the lower deliveries with specific good margin on the models that we delivered combined with a higher participation of the service and parts that led us to this higher gross margin.

And also, services in Commercial Aviation also helped. But we shouldn't consider that as a trend for the whole year. We will be back to what we indicated before throughout the guidance that we send out. But basically, that's what you should work on.

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

Maybe help us understand - so what you're talking about is the guidance of the EBIT margin, but maybe help us understand some of the pieces. For example, the G&A was lower than it's been. Presumably, that's helped by the real. And where should we expect this gross margin? Because just as we look at that quarter, the delivery mix is certainly

going to get better as we go through the year. So is that gross margin going to be lower than the first quarter, even though the real is basically going the right direction and the mix looks like it's going the right direction?

### **A - José Antônio de Almeida Filippo**

Yes. I think that the gross margin should be lower than what we had in the first quarter, like you said. Definitely, the expenses are being positively affected by the exchange rate.

We said that before, that there is a potential benefit if the exchange rate remains in that higher level. And that's what we expected. But basically, I don't think that the margins of the first quarter should be something that should remain, when we take the whole year. Again, we are still relying with our expectation that we indicated early this year when we released the guidance figures.

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

You mentioned - this is the last one - you mentioned that service was a plus for both biz jets and commercial. Can you maybe give us a little bit of specifics, in terms of how much the service business was up year-over-year in the quarter and approximately where it would go for the remainder of the year?

### **A - José Antônio de Almeida Filippo**

Normally, again, I just mentioned - I mentioned that and specifically I think the higher impact was in the executive jet business. Typically, 10% of the revenues are service and parts. We have 24% in this quarter, and that brings a little bit higher margin.

But I think it's so much specific for the quarter, which again we shouldn't expect. The seasonality of this business will probably be more into the deliveries itself, rather than service and parts, going forward. It's just like the situation that we had in the first quarter.

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

Thank you very much.

### **Operator**

Thank you. Our next question comes from Noah Poponak of Goldman Sachs. Your line is now open.

### **Q - Noah Poponak {BIO 16071528 <GO>}**

Hi, good morning, everyone.

### **A - José Antônio de Almeida Filippo**

Good morning.



**A - Eduardo S. Couto** {BIO 18009973 <GO>}

Good morning.

**Q - Noah Poponak** {BIO 16071528 <GO>}

Can you just talk about how you're able to not change the total revenue guidance, given what transpired in the Defense business and the impact from FX there?

**A - José Antônio de Almeida Filippo**

Noah, I think the guidance for the revenues again, we still maintain that with the expectation that the Defense business should be affected from the exchange effects. That already impacted the guidance if you compare to last year figures of Defense. But this first quarter is something that we made this adjustment like we mentioned. That impacted the revenues. That shouldn't be - we don't expect to see that in the current quarters. So that's probably why you are seeing that. But we are still keeping this projection that we indicated before.

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

Maybe I could add, Noah. We are still under the assumption that the main program, the KC-390 - there are three main programs, this is around the KC-390, and the satellites. They will be - one way or the other, they will be kept integral. So we are under that assumption.

We will for sure have a reduction in the base and maybe even the quantity of the modernization programs. So yes, that goes straight to your question. So there will be a reduced revenue there, but that's not the most important piece of it.

On the other hand, we have some prospects of exports of Super Tucano, which at this point, we believe may offset any eventual reduction on the Brazilian side. So I think the best view that we have at this moment is to maintain the guidance, again with the three big assumption - with the big assumption those three main programs being kept intact.

**Q - Noah Poponak** {BIO 16071528 <GO>}

Okay. And there is no change to your assumption for the real in the outlook. Is that correct?

**A - José Antônio de Almeida Filippo**

We based as we disclosed to you at BRL2.8. It's all the way up to BRL3.2; it's now back to BRL2.9 or something, right, I didn't see it today.

**Q - Noah Poponak** {BIO 16071528 <GO>}

Yeah. BRL2.99.

**A - José Antônio de Almeida Filippo**

Yeah. So the forecast in Brazil, they're all over the place, from BRL2.80 to BRL3.10. So we should be – so if we have any risk there, it's probably a little bit of an upside risk.

**Q - Noah Poponak** {BIO 16071528 <GO>}

Okay. And Fred, you mentioned that you missed a few executive jet deliveries in the quarter. Can you just elaborate on that? Is that just purely random timing? Or was that customer choice to defer? Or what happened there?

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

To be totally transparent, we had, I think, two or three airplanes with customer just kind of a few weeks deferral. We also missed, I think, a couple of airplanes in production, believe it or not, which is not – hasn't happened for some – probably some supply chain issue or something.

But – so we should see probably four or five airplanes that what we missed in the quarter. So we're talking about \$100 million to \$120 million, more or less, which should be added onto to the revenues of the first quarter. So that of course impacted negatively.

**Q - Noah Poponak** {BIO 16071528 <GO>}

Okay. So will all of the Legacy 650, Phenom 300, and Phenom 100 have deliveries down this year? And anything you could say about what you think those do next year? Just kind of the Legacy airplanes.

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

I'm not sure I get the question, Noah.

**Q - Noah Poponak** {BIO 16071528 <GO>}

I guess the executive jets excluding the Legacy 500 and Legacy 450, are they down this year? And then, are they down or up next year?

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

Yeah, we don't really disclose that as – in a forward way. So we really group them together. The four models, the Legacy 450, Legacy 500, the Legacy 650 and the Lineage 1000. And we would prefer to stay as a block large aircraft. We never disclose and I don't think nobody does. I don't think anybody does disclose model-by-model, as far as giving forecasts for deliveries.

**Q - Noah Poponak** {BIO 16071528 <GO>}

Yeah. Okay. Thanks very much.

**Operator**

Thank you. And our next question comes from the line of Derek Spronck of RBC Capital Markets. Your line is now open.

**Q - Derek Spronck** {BIO 17904184 <GO>}

Good morning. My first question is on the business jet side. Are you seeing any improvement in the used business jet market in terms of both pricing and inventory levels?

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

Hello, Myles. A little bit of a - Derek, I'm sorry, a little bit of a recovery in the U.S. market, not substantial though, and the rest of the world, no real change to our last report, which is, of course, China was a very important market, which significantly slowed down and the Brazil, particularly for us was also an important market, which also slowed down. So what has been offsetting this is the U.S. market has been growing. So it's pretty much the same picture as we reported a few months ago.

**Q - Derek Spronck** {BIO 17904184 <GO>}

Okay. And the Legacy 500, how is that resonating with your customers? And then in particular, what regions are you finding the most, I guess, interest on that product right now?

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

As far as a percentage, the U.S., for sure. But we, last week, we closed one in Brazil and one in Australia. So it's really gaining traction. And we are not, if you remember when we disclosed our guidance for the year, some people were a bit frustrated by the number. They expected higher numbers. We are really trying to have a very solid ramp-up and in service support, entering into service support. But frankly, it's all over the world. But as far as bulk of demand, it is also in the U.S.

**Q - Derek Spronck** {BIO 17904184 <GO>}

And if I could, the Phenom product line has been very successful and you've sold quite a few. And I guess the pricing reflected that, as well, in terms of getting the good value for your money and as such gathering quite a bit of market share over the past few years. Is that the same sort of strategy you're going to roll out with the Legacy 500 and 450, are you going to try to be a little bit stickier on the pricing front?

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

That's a good question, Derek. The Phenom 300 is the market leader in its segment, by far. And it is the most expensive airplane in this segment. So this is the perfect - when you find the perfect sweet spot for a product. It's a desired aircraft.

The Legacy 500, we see with the potential to become exactly the same in its segment. We are indeed facing, and I have commented on that before, facing price aggressiveness

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from some competitors with larger aircraft than the Legacy 500s, coming down to let's say, the Legacy 500 segment.

But we have been very disciplined to hold our pricing. This is a brand new product. It's probably the most updated, most modern aircraft out there today. And so, we are really trying to hold our price, to develop the airplane. We will not jeopardize an airplane, which has decades of perspective for this short-term pressure.

But having said that, I mean, we're getting a very good resonance about the acceptance of the aircraft. People see the value of the aircraft, and they are gradually coming to accept to pay what we think is the right price for it.

### **Q - Derek Spronck** {BIO 17904184 <GO>}

Yeah. That's great color. And if I could, just quickly on the regional commercial side. I know the E-190, E-195 doesn't compete directly with the CSeries, but there obviously would be some overlap in some of the tender activity out there for the airlines.

As the CSeries kind of becomes more closer to launching into production, are you seeing airlines kind of shifting a little bit more positive towards that program or is it becoming more competitive? And also, how is Bombardier positioning that from a pricing perspective? Are they being as aggressive with the pricing as they have been with their CRJ lineup?

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

Well, we are - if we separate just for a moment, let's say, the regional market, let's say, the typical regional market, the 70-seater, 80-seater, to the larger aircraft, so there is activity going on for the E1 - let's say, our E1 and, of course, the CRJ, there is activity going on.

We are optimistic with a few campaigns, and we see campaigns actually all over the world not only in the U.S. We have this great success at KLM announced last month, I think. And we may have a couple of other contracts, which we will be able to announce some time not in a distant future.

Boeing and Airbus, they have really been very successful in securing a long backlog for its CEO and NEO versions or current and max versions. So what we see is that the airlines that there is a huge commitment as far as narrow-body for the next several years with Boeing and Airbus.

So the impetus of looking at into smaller planes such as our E2 or the CSeries, it's more or less on the - maybe closer to the Boeing and Airbus than what we are. So I think that's the real issue. I mean, there is a lot of capacity already taken by the A320 family and the Boeing 737 family. And the airlines - they are still - they don't need to make a strong move at this very moment.

So that fits, I mean, nicely for us because we will not be in the market until 2018 anyway. But it's an uphill for anybody trying to get new orders from airlines, which have their hands full with huge orders from Boeing and Airbus. This is more or less how we see the competitive market.

**Q - Derek Spronck** {BIO 17904184 <GO>}

That's great color. Thanks a lot. I appreciate it.

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

Yeah.

## Operator

Thank you. Our next question comes from Myles Walton at Deutsche Bank. Your line is now open.

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

Thanks. Good morning. Hey, Fred. I was hoping to just follow up on that last comment you made around the campaigns in the near-term. So it was good to see one non-U.S. campaign hit with KLM. Are they also outside of the U.S., and would they come as soon as Paris?

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

Well, hopefully. Myles, as you know, we cannot make – probably I said too much already. But, yeah, at least – we are optimistic about at least one outside the U.S., maybe something in the U.S. as well. Timing, always depends on the customers. But it is at the point that it makes us feel good about it.

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

Okay. That's good. And then, the other – you mentioned about the business jets missing a couple of deliveries. Production maybe didn't click the way it was planned to this quarter on the supply chain. Was that on the Legacy 500 or, was it on one of the more mature programs?

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

I don't know. Does anyone know? I think, Myles – well, I should – probably I should get you a more precise answer later on, but I think it was the Legacy and the Phenom, I think, but it was a question of days or maybe a couple of weeks. So it's not a big deal. I was just trying to be precise in what I was saying.

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

I appreciate the transparency, Fred. And then, the last one was on the \$30 million in D&S in the quarter that you called out as being kind of a true-up to the FX effects on your programs. Just want to clarify that was revenue not profit. Correct?

**A - José Antônio de Almeida Filippo**

Yes. That is.

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

So what was the profit impact, or the EBIT impact?

**A - José Antônio de Almeida Filippo**

No, the \$30 million is profit.

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

Okay. What was the - okay. So was it a drop through on both, the ?

**A - José Antônio de Almeida Filippo**

Actually, it reduces revenues and profits.

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

Okay.

**A - José Antônio de Almeida Filippo**

But the amounts are very close, close to \$30 million both.

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

Okay. All right.

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

Thank you, Myles.

**Operator**

Thank you. Our next question comes from Ronald Epstein, Bank of America Merrill Lynch.  
Your line is now open.

**Q - Kristine Tan Liwag** {BIO 16493633 <GO>}

Hi. Ron is actually on an airplane right now. So this is Kristine Liwag calling in for him.

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

You have changed your voice, Ron.

**Q - Kristine Tan Liwag** {BIO 16493633 <GO>}

So the question we have is, so the development work on the KC-390 rolls off this year. And if all goes along to your schedule, development work on the E2 should also end by 2020. With a very experienced engineering team, where do you think the opportunities will be next? Is it large-cabin business jets, next generation turboprop, small twin-aisle, small tactical fighter jet? I mean, where do you think future growth for the company will come from?

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

That's a billion-dollar question, right? That's an issue that my team and my board are all of course thinking about. So we will see. I mean, I really cannot tell you now and we have, of course, ideas and we have plans and possibilities. We really have to focus on execution. We have a lot in our plates at this stage. We have never done that many number of programs in parallel. But be sure that it's top of my list what do we do with this capacity going forward.

But we have - I'll just benefit from your question to say, for example in business jets, maybe I can give a little bit more color. My real focus there for the short-term and mid-term is really to consolidate the business, make sure that our Melbourne operation achieves its full potential. As you know, we are also going to produce the Legacy 450 and Legacy 500 in Melbourne. Consolidate our customer support infrastructure and frankly, boost our cash generation from that business. We have to have that cash generation to support our investments in the commercial jets. So that is as far as I can tell you. But beyond 2017 and 2018 when we start to have some availability, that's something we have to sort out in the next probably 18 months to 24 months.

**Q - Kristine Tan Liwag {BIO 16493633 <GO>}**

Okay. Great. And then, on biz jets, when you look at the orders that you have right now in your book, what percent of that is in the U.S. versus international? And then, in terms of where you think orders will come from, is it also U.S. or what's the split between U.S. and international?

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

I don't think we divulge and I would not know anyways. But as far as new orders, the U.S. is the main source of new demand. But a snapshot of our backlog today, I would not know.

**Q - Kristine Tan Liwag {BIO 16493633 <GO>}**

Great. Thank you.

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

Thank you.

**Operator**

Thank you. Our next question comes from Stephen Trent of Citigroup. Your line is now open.

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

Hi, good morning, guys, and thank you for taking the questions. I guess firstly, what is your view of commercial aircraft demand from the U.S. airlines? I mean, you already kind of touched on it, but in addition to the Republic order, do you see like maybe like United Airlines getting interested? Or do you see the legacy carriers more looking at used planes instead of ordering new ones? Do you have any color on this?

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

That's the first?

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

Yes.

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

Okay. Bom dia, bom dia, Steve. Good morning.

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

I'm sorry. This is Kevin, instead of Stephen Trent.

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

I'm sorry, Kevin. That's why I didn't address in Portuguese. Waiting for the usual bom dia in Portuguese. But I'm sorry. Yeah, we see a continuous activity in the U.S., definitely for the E1. We cannot mention any names of course. We announced those five for Republic recently and there are - I mean, there are an outstanding number of options there. And the airlines, as soon as the faster they can replace their 50-seaters, the more they're going to order aircrafts.

So we are probably bullish about seeing the potential in the U.S. and our ability to compete. We believe we have a good product. And the experiencing service of the recently delivered E175s with improvements has been excellent. So everybody who is flying the airplane, this new version of the airplane, is really, really thrilled. So that creates a virtual circle and hopefully we will keep us in the lead to satisfy that demand.

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

Okay. Great. And I guess just coming back to the KC-390 development program and all the other ones that you have on your plate, you said you've never really had this many projects all on line at the same time in developing. If the payments from Brazil's government continues to get delayed, do you have any options to continue funding the development? Or, I mean, could you see something similar to what Bombardier had to do with the Learjet?

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



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Well, in the KC-390, KC-390 is a key program. So I definitely do not see Embraer funding the program. So let's say, the current - the best picture we have today is the continuation of the program, as planned or, close to as planned. But also, we have to consider a less optimistic scenario where there is a slowdown and a stretch-out of the development phase. That's a possibility, and we are discussing with the government very openly and fundamentally with the standpoint that either they are able to sustain the current pace of development or if they are not, you really need to sit down and reprogram it.

We do not see any scenario where the airplane is dropped out. It's just - we are way down the roads. It would be a really not very smart to stop this program at this stage, having the first prototype already in flight and almost the whole development done. So what is there is the flight test campaign, two more years to go. And so we do not see a scenario where we're going to just stop the program.

So the worst-case scenario is our perspective would be a slowdown and re-dimensioning of the program, which of course then we would adapt ourselves on the cost side to cope with that. But that's not what is there today. Today, the discussion is still how to preserve the program as it is and how do we get the late payments, fundamentally.

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

Okay. Very helpful. And then, finally, just circling back on, I guess, unit margin, you talked about, I think, the biz jet side. On the commercial segment, margin change year-over-year, do you know what portion came from higher production levels versus, I mean, any FX effects on like SG&A and costs?

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

A combination of things, I think.

**A - José Antônio de Almeida Filippo**

We had a couple of things. We had the FX that helped us on Commercial Aviation. We also had the higher delivers, right? We delivered 20 E-Jets versus 2014 last year. And also, we also had some efficiency gains as we only deliver the E175. So we have been mentioned that we increased the mix of E175s even though it comes at a lower price. We have efficiency to gain as far as production, and that's what we are showing in the results. So I think it's a combination FX, efficiency gains, and the higher delivers that we had in the quarter.

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

Okay, thank you. And like how much would you say it was from efficiency gains and how much was from FX?

**A - José Antônio de Almeida Filippo**

We cannot disclose that. We don't have that prepared. But basically, it's like we said, it's a combination of that. It depends on the number on the specific period that we deliver. So it's all together. That's how we approach that.

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

Okay, great. Thank you very much.

## Operator

Thank you. Our next question comes from Alexandre Falcao of HSBC. Your line is now open.

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

Hi, good morning. My question is regarding if there is any delays on in Defense. In terms of accounting, how are we going to actually see this flowing through results? What I mean is, if we see some sort of contingency in the government, does this mean that you guys are going to cut the revenues from this or going to maintain revenues and just book it as more receivables? So I'm just trying to see exactly if there is any delays specifically on the big programs how we're going to see this flowing through results? Thank you.

**A - José Antônio de Almeida Filippa**

Alexandre, actually the way it works, those type of contracts they are recorded as a percentage of completion. So normally, as you advance in the development of the program you recognize the revenue. So the impact if for some reason this program will review its schedule, for example, then there's going to be like lower deliveries, because of the percentage of the advance of the program, which we don't expect, as Fred mentioned, that should happen.

So that's typically how it works. It's not a question - we're not invoicing, for example. It's just like more percentage of completion, advancing, then it's recognized as revenues. That's how it works.

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

Okay. But would you stop the - because I know you guys are in the final stages, almost flying this aircraft right now. Would you continue the completion, even if you don't receive any money from the government?

Just I'm trying to understand if that is, because in the press, each and every day there is a news that the Finance Minister and the Planning Minister are going to announce a big budget cut, or at least a budget contingency. So just wanted to see how this - if any, if there is going to be any impact in the P&L here?

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

Well, the answer is, no, we will not continue without the proper applicable payments. I mean, there is a delay, of course. When they stopped paying us, we did not stop the activities for a few months. So we have not stopped so far, under the belief that they will resume their payments and eventually normalize that very unfortunate situation.

If the cuts are permanent, we have no other option than to stop it. But again, I don't think this is the likely scenario. It would not be – that's a not a very smart place to cut, frankly, because this is a needed airplane. It's a potential source for exports. But theoretically, if that happens, yeah, we will not fund – we cannot fund the rest of the development by ourselves. We will not do that.

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

Okay. Thank you so much.

## Operator

Thank you. Our next question comes from George Ferguson of Bloomberg Intelligence. Your line is now open.

**Q - George Ferguson IV** {BIO 20358806 <GO>}

Thank you and good morning. As I look at the backlog for the E2 program, it doesn't look like there's been any successful campaigns in the last two quarters to three quarters. So I was wondering if you could catch us up with how campaigns are going for the E2 program right now?

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

Okay. That's a fair question. There is a lot of activity, and I just refer back to a previous question. We had a very good start at the launch of the program, with bulk of launch orders. And the airlines, as we are still relatively far from first deliveries, three years from first deliveries, the airlines having a lot of orders for Boeing and Airbus products, they are comfortable in waiting a little bit more. So that's kind of the background.

Having said that, we do have a lot of activity. We have several campaigns going on around the world at different stages. But we are not particularly anxious about the very short term, because first we have this bulk of launch orders, which take several slots from the initial delivers. And, second, because we understand that there is this outstanding backlog for Boeing and Airbus, which reduces the appetite for the airlines for short-term commitments.

**Q - George Ferguson IV** {BIO 20358806 <GO>}

Okay. Thank you. Is there a timeframe we should think about where we'd start to see E2 orders be re-energized here? Is it a couple of years out, or how should we think about the sort of the timeframe?

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

Yeah. As we approach the entry into service, which is 2018, of the first model, probably it's reasonable to see some more activity within the 24 months before delivery. So sometime next year, probably. That's sounds right.

**Q - George Ferguson IV** {BIO 20358806 <GO>}

And are you seeing your airline customers change any of their thinking around new generation technology versus older, less fuel efficient technology? I mean, do you see any sort of shift there? What's - how is that affecting things, do you think?

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

That's a point, actually, that I failed to remark. With the recent decrease in oil prices, that has also, let's say, slowed down the urge for replacing aircraft. I don't think we can call it a trend, yet. It's a very short-term effect, very short-term development. But the airlines, everybody, I think, the industry is kind of a wait-and-see mode to see where oil will go.

Let's say, if the oil stays at current levels, there will be, of course, less impetus from the airlines to race and change aircraft. But in the long-term - mid- to long-term, it's - I think it's an absolute certainty that the new airplanes, the new engines, the new generation of aircraft will dominate the picture.

**Q - George Ferguson IV** {BIO 20358806 <GO>}

Okay. Thank you very much. I appreciate it.

**Operator**

Thank you. And our next question comes from the line of Bruno Amorim of Santander. Your line is now open.

**Q - Bruno Amorim** {BIO 17243832 <GO>}

Hi, good morning. I'd like to know if in your opinion, the 13% EBIT margin in Commercial Aviation could be seen as a floor for the full year? Because you said that what helped in this quarter was FX, higher deliveries, and efficiency gains. FX is still at BRL3. You are going to deliver even more aircraft on a quarterly basis in the upcoming quarters according to your guidance. And I guess efficiency gains will still be there. That's my question. Thank you.

**A - José Antônio de Almeida Filippo**

No, Bruno, I think that this is not a floor. I don't think we should consider that. Although that should be considered that the important is the whole year. This is a combination of things that affect. FX is also always important, dilution like we mentioned before and some efficiency gains.

Sometimes you can benefit more or less on that, depending on the activity on the quarter. So I don't think that could be considered necessarily as something that should replicate going forward. I think that you should consider that back to the guidance range that we indicated in terms of revenues, I think will be the best way of -

**Q - Bruno Amorim** {BIO 17243832 <GO>}

Okay. Thank you.

## Operator

Thank you. And I'm showing no further questions at this time. I'd like to hand the call back over to José Filippo for any closing remarks.

## A - José Antônio de Almeida Filippo

Okay. Again, I'd like to thank everybody to join us. And of course, our IR team is always available. So if you want to go forward into some questions, we'll be ready to attend you. So thank you very much, and have a good day.

## Operator

This concludes today's question-and-answer session. That does conclude Embraer's audio conference for today. Thank you very much for your participation. Have a good day.

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