

Q1 2013 Earnings Call

Company Participants

- Frederico Curado, CEO
- Jose Filippo, CFO
- Luciano Froes, IR

Other Participants

- Amit Mehrotra, Analyst
- Cai Von Rumohr, Analyst
- Darryl Genovesi, Analyst
- Joe Nadol, Analyst
- Noah Poponak, Analyst
- Peter Skibitski, Analyst
- Ronald Epstein, Analyst
- Stephen Trent, Analyst
- Turan Quettawala, Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to the audio conference call that will review Embraer's First Quarter 2013 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. (Operator Instructions) 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 believe, may, will, estimate, continue, anticipate, intends, expects.

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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 lights of these risks and uncertainties, the forward-looking events and circumstances discussed on this conference call might not occur. The Company's actual results could differ substantially from those anticipated in the forward-looking statements.

Participants on today's conference call are Mr. Frederico Curado, President and CEO; Mr. Jose Filippo, Chief Financial Officer and IRO; Mrs. Elaine Funo, Director, Tax Accounting; and Mr. Luciano Froes, Director of Investor Relations. I would now like to turn the conference over to Mr. Frederico Curado. Please go ahead, sir.

Frederico Curado {BIO 2004589 <GO>}

Good morning, everyone. I will -- I'll just turn this to Filippo. So he can make the formal presentation. And both of us, plus Luciano, will be back at the end for Q&A. Thank you.

Jose Filippo {BIO 1726218 <GO>}

Okay, thank you, Fred. We're going to go through the presentation of the First Quarter of 2013 results, starting on page three with the highlights of the business, starting with the Commercial Jet business. We had the delivery of 17 E-Jets in the First Quarter of this year, which led us to reach the total of 925 aircrafts since the entering to service.

We had a confirmation of the Republic deal. Last time, we mentioned about the need for confirmation, approval from the court in the US. And that happened in the end of March. So now it's already included in the First Quarter backlog just announced.

Important as well would be new contracts with important customers for parts, service, management and logistic solutions. So with Republic, Azul and Trip. And the continuing of the program for the new generation of the E-Jet, as communicated, we continue to announce main suppliers for the project. At this stage, we have most of the main suppliers already selected.

And to finalize the highlights in the Commercial Aviation, the announcement of the sale for two E-190 for Austral Lineas Aereas. It is also included in the backlog of the First Quarter in the end of March.

Going to page 4, regarding Executive Jets highlights, the delivery of 12 jets in the First Quarter, typical -- reflecting a typical seasonality. But it's important that we had the good mix, where we had participation of large jets, four large jets in the deliveries of this quarter.

Regarding Phenom 300 capabilities, it's important confirmation of this aircraft highlights with the record of three speeds for the lightweight class that happened recently. Also, an important recognition of quality and value proposition of the models Legacy 500, 450 and 650, was honored by luxury press Hurun Report from China.

The program of the Legacy 500 has an important milestone, which was the third prototype flight that happened recently. And we still keep the projections for expecting to deliver by the first half of 2014.

Concluding the highlights for Executive Jets, we've had the information of the sale of one Lineage 1000 in China.

Next page, on page 5, regarding Defense and Security, the KC-390 program, another important milestone was reached, with the conclusion of the Critical Design Review. And we have the expectation of the first flight for the second half of 2014 on track of our expectations. Two important announcements of commercial activity, sales for Guatemala and Senegal, of aircraft, Super Tucanos. And also, surveillance and protection systems.

Regarding the LAS program, we are moving forward with the activities. And we had the opening ceremony of Jacksonville facility, where those airplanes will be manufactured.

Concluding the Defense and Security highlights, another support contract, Brazilian Air Force, for the existing Super Tucano fleet.

That will conclude the highlights. And we start on page 6, information of aircraft deliveries. In the chart on the left, Commercial Jets, we had 17 deliveries in the First Quarter. We missed a few aircrafts in the First Quarter. But expect to have this delivered in the Second Quarter. This is following a typical pattern. We expect to improve this in the Second Quarter.

If we go to the chart on the right side, the Executive Jets, 12 deliveries in the First Quarter. As well, the seasonality impact. We had -- we faced some customer financing delays. That will be resolved soon. So expect to have a stronger Second Quarter in terms of delivery.

And to conclude the deliveries, we're just confirming and keeping our guidance for 2013, which is shown in the table in the bottom of this page.

Moving to next page, page 7, the backlog, we had an amount of \$13 billion for the end of the First Quarter, an increase from the Fourth Quarter of last year, primarily because of the Republic deal in the Commercial Aviation, as well as some contracts in the Defense business.

Page 8, the same information of revenues, the information on revenues. By segment, we have the total in the left, top left chart, the total of \$1.086 billion of revenues in the First Quarter, slightly below the First Quarter of last year, primarily as a result of aircraft deliveries in the Commercial Aviation. But this was partially offset, if we see each chart for each business, partially offset by the growth in Defense and the Executive Aviation business. So we accounted for a total of \$1.086 billion in the First Quarter of this year.

Next page, page 9, is the consolidation of the revenues in dollars and Brazilian reais. We had then this amount of \$1.086 billion in the First Quarter. And we are keeping our

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guidance figures for the year, a range of \$5.9 billion to \$6.4 billion for the full year of 2013.

Going forward, next page, page 10, talking about expenses, information in reais and in dollars. We had a total of \$161 million SG&A expenses for the First Quarter. It's a reduction compared to the last quarter of last year. And also compared to the First Quarter of 2012. And we see Commercial Aviation stable in terms of selling expenses, with a reduction in the G&A. And the main drivers, as we did a focus that we've been putting into cost reduction and controls, coupled with the dollar impact. And also the stimulus package, which been reducing some of the expenses.

Next page, page 11, income from operations. We had a total in the left, total income of \$40 million for the First Quarter of this year, with a 3.6% operating margin. Although we had a typical weak quarter, we had some important considerations impacting those figures, which is the lower revenues and gross margin, combined with some -- with two non-recurring items, which basically, provisions made for labor disputes. And accounting implementation of retroactive selling adjustments, the (inaudible) that we have in 2012. So these two adjustments combine to the lower gross margin, returning to a lower margin for this quarter.

Also important to remind that if you compare to the First Quarter of 2012, we had to consider that in 2012, we had important liquidation damage revenues here that impacted positively the expenses and the operation income in last year. So that also impacted the comparison from both quarters.

And regarding the guidance, we're keeping our projections, with a range of \$530 million to \$610 million, with a margin of 9% to 9.5% for 2013.

Next page, page 12, in terms of EBITDA, we have a total of \$100 million in EBITDA for the First Quarter, a margin of 9.2%. And this is basically the reflection of all the mentioned -- the already-mentioned impacts in operating margin. That is reflected here.

For the EBITDA, we're still also keeping on track on the guidance for 2013, with a range of \$770 million to \$900 million for EBITDA for the year, with a margin in the range of 13% to 14%.

Next page, page 13, net income, total of \$30 million in the chart on the left for the quarter, with a gross margin of 2.8%. We don't -- we didn't have major effects of exchange rate for this quarter. So it's basically the consequence of the margins that we mentioned -- the facts that we mentioned before. So a total of \$30 million, 2.8% net margin for this quarter.

On page 14, talking about inventories, we had a total amount in the end of the quarter of \$2.5 billion, in line with our expectation. We had a typical increase from year-end figures. And we see that we are slightly below the First Quarter of last year. So we're still on track. So we're confident that we have a good control and monitoring of inventory, which is key important for us in terms of the results.

Next page, page 15, the free cash flow. We had a weak First Quarter, negative of \$205 million. Some considerations. Basically, operating activities is associated to some missed deliveries, with costs, some increase in inventories. And some payments related to guarantees of American Airlines' restructuring, a total of \$66 million.

And regarding the intangible increase, mostly associated to the development of the Legacy 550 and 500 model.

In terms of CapEx, \$68 million -- sorry, \$50 million, in line to expectations. We expect to see improvements in the next quarter. But still negative, with a recovery in the second half. It's good to remind that for the full year, we expect positive cash generation of double digit for this year.

Next page, page 16, in terms of the investments, the breakdown. As we see here, we have -- we're on track and in line with our projections. Year to date, \$134 million, broken by \$21 million in research, \$61 million (sic -- see Company presentation) in development. And \$45 million in CapEx. For the full year, we're keeping our guidance of \$580 million for 2013.

The last page, in terms of our capital structure, we feel we have in the left, we have a debt with comfortable profile. We have increased our long-term portion. And we had a strong cash position of over \$2.5 billion position. So, this is the profile of our debt.

And with that, we finish the presentation. And then we open for questions. Thank you.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from Noah Poponak of Goldman Sachs. Please go ahead.

Q - Noah Poponak {BIO 16071528 <GO>}

Hi. Good morning, everybody.

A - Frederico Curado {BIO 2004589 <GO>}

Good morning, Noah.

Q - Noah Poponak {BIO 16071528 <GO>}

Just wanted to follow up on the reiteration of the margin guidance. You know, I know the past several years have had a fairly back end loaded EBIT and EBITDA contribution. But now to get to the range for the full year, it looks severely back end loaded.

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I just wondered, first, as a clarification, is the reiteration including the one-time items in the quarter, meaning you're getting there despite those one-time items? And then secondarily, can you just maybe talk about the degree to which this quarter's margin was what you thought it was going to be when you first put out that guidance. And just the level of comfort you have in reiterating the full year target? Thanks a lot.

A - Frederico Curado {BIO 2004589 <GO>}

Okay, Noah. So trying to combine the two questions. Yes, we still feel comfortable with our predictions, with our guidance. Yes, we had a little bit lower margins than we expected, for two reasons. One, we missed a few deliveries. So a handful of deliveries, Commercial aircraft. And the two deliveries also in the Executive Jets business. So that -- you know, (inaudible) did not contribute, dilute our fixed costs. And we had these non-recurring events as Filippo mentioned.

We will have a back-loaded year. We will have probably a -- I'd say a higher load, the back of the year, than we had last year. Last year we had a more calibrated flow throughout the year. But again, the number still show -- still makes us believe that we're on track for delivering those results.

Q - Noah Poponak {BIO 16071528 <GO>}

Are you expecting to get into the ranges even after the negative recurring items you took this quarter?

A - Frederico Curado {BIO 2004589 <GO>}

Yes, they didn't -- of course, they were not expected. But they are not -- you know, when you consider the whole year, they are not that material. And we always have some -- also, some positive surprises that may offset that. So I think it's too premature -- it would be too premature to throw the towel on that. So we are still firm on those numbers.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay. Great. And then, I just wanted to ask one other thing, on the light cabin Business Jet market, broadly, we all saw what Cessna announced a couple of weeks ago. You mentioned fewer cancellation penalties, at least, which is somewhat positive, I guess, in the quarter. Can you maybe just touch on what you're seeing broadly in terms of demand trends. And how you're seeing -- and how what you're seeing compares to what Cessna said a couple weeks ago? Thanks.

A - Frederico Curado {BIO 2004589 <GO>}

We are -- I mean, we do not dispute this is a tough market. It is the toughest segment of the Executive Jet market. We have in our 89 aircraft delivery guidance, we have a higher load of Phenom 300s, which are selling well, lower quantities of Phenom 100, which is the hardest part of the market.

We don't have 100% of our aircraft sold. But we have probably between two-thirds and three-quarters of those airplanes sold. Two factories, one in Brazil, one in the United

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States. So we -- again, it's not a walk in the park. But we firmly believe it's due. So we're sticking to our delivery target as well.

So maybe driven by the Phenom 300, which is really outselling everybody in the segment. It's just a very popular aircraft.

Q - Noah Poponak {BIO 16071528 <GO>}

Okay. Thanks a lot.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

Operator

Our next question comes from Joe Nadol at JPMorgan. Please go ahead.

Q - Joe Nadol {BIO 3056499 <GO>}

Thanks. Good morning. So, let's dig into the gross margin, specifically. If we adjust for the settlements, your gross margin was still down a little bit. And it's been my sense, certainly, that the Republic and now the United orders are probably going to be dilutive when they start. And they haven't started delivering yet. So -- and then, of course, you have the big payroll tax item, which has been a big help.

So could you give a little bit better sense as to how all those items combine when you look forward from, say, the 22.7, ex the settlement this quarter, as we look sequentially forward, do you expect dilution? Can we hold it flat? What do you expect?

A - Jose Filippo {BIO 1726218 <GO>}

We expect to have, of course, compensation, because we had a weak quarter. For example, in terms of the impact compared to last year, in terms of lower gross margin revenues, we had a 2.5% reduction in the operating margin. The provisions were 0.9% impact. So we see that, in terms of the expenses, it should be one time. We don't expect to see that going forward. And for the gross margin, we see maintenance of that, that amount.

So we still work on a projection close to the number that you mentioned for the full year, which will, of course, with the higher delivery amounts going forward.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay. Can you quantify what the benefit in the quarter was from the payroll tax?

A - Jose Filippo {BIO 1726218 <GO>}

The payroll -- the total of the payroll tax, about \$8 million -- sorry, \$18 million.

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Q - Joe Nadol {BIO 3056499 <GO>}

Okay. And then on the cash flow, Filippo, I think you mentioned that this was -- I didn't quite catch it. But that in that number was a payment on the -- some of the guarantees. Was that -- could you just repeat that?

A - Jose Filippo {BIO 1726218 <GO>}

Yes. That's not -- it didn't impact the margin, because already, we had a provision for that. It's more --

Q - Joe Nadol {BIO 3056499 <GO>}

No, I understand. But -- yes, I'm changing the conference to cash flow now.

A - Jose Filippo {BIO 1726218 <GO>}

Yes, the cash flow. This was -- let me get the number directly. It's about \$60 million impact.

Q - Joe Nadol {BIO 3056499 <GO>}

\$60 million, okay. And you mentioned that -- I think you mentioned that free cash flow would be negative in Q2. But better? And then, positive in the second half. And positive for the full year overall? Am I getting that right?

A - Jose Filippo {BIO 1726218 <GO>}

Correct, that's what we mentioned. We expect to see it recover. But still negative in the short term. Here, two digit positive cash flow.

Q - Joe Nadol {BIO 3056499 <GO>}

Two digit, okay. Okay. And then just finally, Fred, congratulations on the order from United. Just wondering, you get this question every quarter, I thought I'd just throw it out there, if you could give your latest and greatest on the outlook for commercial aircraft, the demand outlook, particularly focusing on the US carriers, of course.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you, Joe, thank you. It was a nice one. Well, let me try to give a helicopter view where we are.

So to date, we've been saying that we estimate that some 300 to 400 aircraft over the next, let's say, year and a half, two years of orders, to be delivered over the next maybe three, four, five years. So if those numbers are correct. So far, we have probably about a third of those orders already committed. If I recall correctly, 40 aircraft for Delta, 47 for Republic. And now 30 for United. So this is roughly 120. So let's say a third. And those three orders, they have a -- the same number of options attached to them. So there's another 120 options out there, which of course, may or may not be confirmed.

So if we take a -- let's say, just an overall balance, we see that 120 aircraft are done. And maybe some 200 to 250 or so to be contracted. And this will be the sources of those new orders, will come from, number one, the existing options, number two, the direct procurement from American Airlines for American Eagle, which is still out there to be decided. And of course, some of the regional airlines, which have not yet done anything in those new category of aircraft.

So, I think we are -- so far, we are doing good. But we still have some room ahead of us. And the battle with -- some important battles still to be fought. And to be won.

Q - Joe Nadol {BIO 3056499 <GO>}

Do you anticipate that some of these battles will happen by the Paris Air Show?

A - Frederico Curado {BIO 2004589 <GO>}

Maybe, Joe. So, I don't know. Maybe. A lot of activity is out there. But as you know, it's not under our control. So we do depend on the customers. And how they run their -- how they get their act together.

Q - Joe Nadol {BIO 3056499 <GO>}

Okay, thank you.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

Operator

Our next question comes from Pete Skibitski of Drexel Hamilton. Please go ahead.

Q - Peter Skibitski {BIO 6760095 <GO>}

Good morning. A couple more questions on margin rate, I wanted to focus on the administrative and selling. Administrative costs were very low this quarter on an absolute basis. I'm wondering if that absolute level of \$50 million and change is kind of your expectation for the rest of the year, or should we expect that to ramp? And selling expenses were roughly flat on an absolute basis year over year. I'm wondering if those should ramp the rest of the year as well with sales, or if those will decline at all.

A - Jose Filippo {BIO 1726218 <GO>}

Yes, that's a bit what we project. We had this number in the First Quarter, in terms of G&A. And we expect to see the same trend going forward. It's not an expectation. But it's good to remind that in the last quarter, we had some pre-op expenses that were accounted that we changed. But it's not material, just for fair comparison. But to still keep that we have this level going forward, which is a reduction. In terms of the selling expenses, it should be flat throughout the year as well.

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Q - Peter Skibitski {BIO 6760095 <GO>}

Excellent. Excellent. Okay, thank you. And then, I guess, Frederico, on the United win, I was just wondering if you could help us out in terms of how we should think about RJ rates in 2014, given the win. And then maybe you could help us out with timing. Will these all deliver in 2014, or maybe split over 2014 and 2015?

A - Frederico Curado {BIO 2004589 <GO>}

Yes, they are. They are -- they start in 2014. I don't have the exact breakdown. But it's 2014 and 2015.

So as far as rates, maybe taking the benefit of your question, which probably, we -- with that order, we pretty much are assured the current level of production for our Company and next year as far as the Commercial Jets. So we -- of course, we are still procuring some new orders. So there is a possibility that we, of course, are getting a few more orders. We can come back to the 2011, 2012 production levels, which is something 10% to 15% above where we are this year.

So it's looking good. And 2014, therefore, is looking good. And 2015, also starting to look good as we get those new orders.

Q - Peter Skibitski {BIO 6760095 <GO>}

Very helpful. Very helpful. And then, if I could, again, the US Air Force last contract, that's obviously been a lot of drama getting that through. And it seems like you're actually doing work on less now. And I wanted to ask you, I think it's 20 aircraft. Do you expect to deliver all 20 in 2014? And if so, I'm guessing your overall Super Tucano deliveries will be very high in 2014.

A - Frederico Curado {BIO 2004589 <GO>}

They also -- that contract is also spread in two years. So we will start 2014. I think we start delivering aircraft in second half of 2014, which will be a -- quite a challenge, because just like 15, it's 15 or 16 months away from now. And we are indeed doing a lot of work already in that program.

So it's going to be 2014, probably more loaded in 2015 than 2014. I don't have again the precise numbers. But we're certainly going to deliver more aircraft in 2015 than 2014, in the case of Tucano.

Q - Peter Skibitski {BIO 6760095 <GO>}

Great. Thank you, very much.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

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Operator

Our next question comes from Turan Quettawala of Scotiabank. Please go ahead.

Q - Turan Quettawala {BIO 6362141 <GO>}

Good morning, (inaudible). I guess, maybe, Fred, I know you talked about a production rate just in the last question. Can you give us a sense of what % of the 2014 and 2015 production is sold on the E-Jets?

A - Frederico Curado {BIO 2004589 <GO>}

Well, if we take, let's say, the current year, 2013 current levels, we have pretty much done for 2014. I would say probably around maybe two-thirds or so for 2015. But of course, we have the ability to ramp up production a little bit up, again, back to the 2011, 2012 levels, between 100 and 120 -- sorry, 100 and 110 aircraft. So some 10% to 15% above where we are.

So if we kept the production stable next year compared to this year, we would be pretty much sold out at this stage.

Q - Turan Quettawala {BIO 6362141 <GO>}

That's great, thank you. And I guess you need, what, 12 months or so just to ramp up production. Is that fair, in terms of the time --

A - Frederico Curado {BIO 2004589 <GO>}

Yes. That's a fair assumption, yes. Of course, there is a limit. So this low is also important. But lead time, (inaudible) correct, yes.

Q - Turan Quettawala {BIO 6362141 <GO>}

Okay. Great. And I just had one more question. I know that the RJs have been the biggest area of opportunity here in the last few months in terms of orders. But I'm just wondering about some of the larger planes. Maybe you can talk a little bit about what's happening in emerging markets with the E-Jets. And also, just as the CS100 becomes more of a reality, are you seeing that come up as a competitor in any of your campaigns?

A - Frederico Curado {BIO 2004589 <GO>}

Well, the activity on the 190, 195 segment continues. In Latin America, we have some activity. We just announced those two extra aircraft for Austral in Argentina. So China is also -- there is some activity going on there, Africa and the Middle East.

So there is not huge size orders. But smaller, some option confirmation, some smaller campaigns. So it's kind of, I think, in the average of that segment of the market.

The CS100, we see, of course, as far as size, it's an aircraft about the same size as our 195. It's -- those are very different aircraft as far as performance. So the CS300 is an

aircraft which is much heavier than the 195. It has longer range than the 195.

So we still believe that -- in the merits of our 195, we still believe that the 195 is really optimized for -- 190, 195, optimized for the mission. And as far as range, recover something like 98% of the average missions in the world. So we don't see the real benefit of this extra range in the CS100.

But again, when it's out there, it's going to be another aircraft fighting for customers. So we, of course, we respect that.

Q - Turan Quettawala {BIO 6362141 <GO>}

Okay. Great. Thank you, very much.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

Operator

Our next question comes from Cai Von Rumohr of Cowen & Company. Please go ahead.

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

Yes, thank you, Fred. And congratulations on the United order.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you, Cai.

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

Is the United pricing comparable to the Republic order?

A - Frederico Curado {BIO 2004589 <GO>}

Of course, I cannot tell precisely. But I would say in the order of magnitude, all those campaigns, I think they have similar price levels. But of course, I cannot campaign or compare -- I mean, comment or compare prices between the two airlines.

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

Okay. And you mentioned of the order potential in the US, the options you have from Republic and United. What is the lead time on those options, i.e., do they have to give at least 12 months' notice? And given that -- as I believe both current orders go -- or at least, the Republic, what, goes through, what the middle of 2014 or a little farther, what's the earliest you could get those options? I mean, because it doesn't look like -- that they would get more in the current timeframe. It would just extend the deliveries. Or would it? Could you get those options sooner?

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A - Frederico Curado {BIO 2004589 <GO>}

Cai, the Republic deliveries, they actually stretch out to 2015. So as of 2013, we start in the second half 2014. And some remaining aircraft in 2015. And their options, they start in the continuation of the last firm order. So it's more backloaded into 2015 and 2016, as a continuous flow of orders.

So the options that we have, maybe, maybe not, I'm not 100% precise here. But we start really to get more heavier loaded from 2015 on, 2015 and 2016 on. So there's not much room. There is some. But not much room for options in 2014.

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

Got it. And then, the Legacy -- my sense is, that's slipped a little bit. And while its entry in service in the first half of 2014, is it more likely to be closer to midyear than the beginning of the year?

A - Frederico Curado {BIO 2004589 <GO>}

I think that's a fair assumption. We always sustain first half. Of course, we realize it's a relatively broad range. And we have been talking about the entry into service. So, we're doing a lot of work to assure that once we get into the Legacy 500 into service, it's really debugged and it's mature. So we're investing a lot of efforts and resources in the flight that's campaigning, maturity campaign, also -- I mean, both in the ground and in flight. So we may have a certification earlier in the year. And would like to enter into service a little bit later.

So we are giving ourselves the six months, let's say, flexibility. But I would agree with your comment that it's more likely to have airplanes being delivered to customers more towards the mid part of the year.

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

Got it, thank you. And then, the Gen 2 really looks, I think, more impressive at this point -- you have the new engines -- than it might have 12 or 18 months ago. Presumably, this also costs somewhat more money. Can you give us any kind of color, if you launch it as -- and presumably you will, at midyear, what -- A, what a rough range of what the development might run. And kind of the profile of when that spending will start to hit your P&L, start to hit your cash flow?

A - Frederico Curado {BIO 2004589 <GO>}

Cai, of course, I would ask you for a few more months to talk about volume. Profile, if we do launch, let's say, this year, which of course is our intention to, working towards that, this starts to get really more loaded in the 2016. And -- so it's a ramp up. For 2015, there is, of course, there would be -- for -- I mean, sorry, 2015 and 2016. So next year, 2014, you will see the start of a ramp up.

So as we certify the Legacy 500 and 450, then we start really moving our engineering resources in higher quantities to the second generation.

So as far as the investment of the Company, we probably should see something flattish. But as far as a program itself, it really starts to pick up in sizable resources, probably installed in 2015.

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

Terrific. Thank you, very much.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

Operator

Our next question comes from Ron Epstein of Bank of America/Merrill Lynch. Please go ahead.

Q - Ronald Epstein {BIO 4430430 <GO>}

Good morning, Fred.

A - Frederico Curado {BIO 2004589 <GO>}

Good morning.

Q - Ronald Epstein {BIO 4430430 <GO>}

Following up on Cai's question, the second generation E-Jets, how -- in the preliminary customer conversations you've had so far, how has the aircraft been received? And vis a vis, say, the CS100, what's your feedback?

A - Frederico Curado {BIO 2004589 <GO>}

Ron, let me talk about Embraer. I don't have any feedback on the CS100. I can tell you that there is -- I mean, real interest in the aircraft. We have to keep in mind that this is not a new aircraft, per se. This is a, let's say, it will be a significant improvement over an existing aircraft, which has 60-plus customers in 40-plus countries. So there is about 1,100 or so aircraft. So the customer base is there. So, we are starting from a solid start -- I mean, from a solid base.

So now that we are really talking to more details with the airlines and leasing companies about the new aircraft, I am encouraged, to be frank, about the prospects of those new second generation airplanes. And it's -- it will be, I think, a very important change in the history of regional aviation, because if you look back at the history of regional aircraft, what we see is segments going up and down, products coming up and disappearing. And we -- I think we will set a new reference now by really extending the life of an existing kind of product.

So the E-Jets family, we see as a family which has a very long -- a very potential longevity. So beyond the current generation, the second generation. And perpetuating our

presence in that market segment.

So I'm really encouraged. And really trying hard to put together the business plan which is sound, as far as returning investment. Market response has been good.

Q - Ronald Epstein {BIO 4430430 <GO>}

Great. And then, following up on another question that Cai asked, in terms of investment (inaudible), I think at one point, I think you said it might be in the range of \$1.5 billion. Is that still right?

A - Frederico Curado {BIO 2004589 <GO>}

I never said that one.

Q - Ronald Epstein {BIO 4430430 <GO>}

Okay. Okay.

A - Frederico Curado {BIO 2004589 <GO>}

I don't recall saying that. Maybe somebody else, somebody did at Embraer. But I really ask you to wait for a few more months. And to get the number. And of course, we'll disclose it formally. And it will be something more solid. But I -- that's where we are.

Q - Ronald Epstein {BIO 4430430 <GO>}

Okay, great, fair enough. And then just maybe switching to the Defense business for a minute, Fred, can you see your 390 program -- we haven't talked much about that on the call yet. How is that going, how's the development going? And are you seeing any other customer interest outside of the existing customers that you already have for it, or potential customers you have for it?

A - Frederico Curado {BIO 2004589 <GO>}

Until we actually fly that, I think there's two events which are very important to run, for -- let's say, for the start of a commercial campaign for the aircraft. First, of course, is the flight of the aircraft, which is scheduled for the end of next year. And very importantly also, is the execution of the contract with the Brazilian Air Force for the delivery of the airplanes. But what you have so far is, there's a development contract.

So once we have a contract to deliver X number of airplanes to the Brazilian Air Force, with a firm price, a firm configuration, everything settled down, we then -- from that reference, we can start selling the aircraft for other customers, starting, of course, with those who have a participation in the program.

And the first flight, also, I think is a key element. So we're able to show the aircraft. So I would anticipate some more commercial activity, more towards like end of next year into 2015. And let's say a stronger pace in our marketing efforts in the aircraft.

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Q - Ronald Epstein {BIO 4430430 <GO>}

Okay. Great. And then maybe just one last question, an operational question. Where is San Jose dos Campos now, in terms of the final assembly cycle on 170 or 190? How many days does it take now?

A - Frederico Curado {BIO 2004589 <GO>}

Maybe Luciano can help me. I think it's 7 or eight days?

A - Luciano Froes {BIO 17907241 <GO>}

Yes.

A - Frederico Curado {BIO 2004589 <GO>}

But let us just cross-check it, Ron. I think we have the information here. Yes. Yes. So my memory is assumed acceptable, seven days is our cycle time for final assembly in our E-Jet hangar.

Q - Ronald Epstein {BIO 4430430 <GO>}

Okay. Great. Thank you, very much.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

Operator

Our next question comes from Stephen Trent of Citi. Please go ahead.

Q - Stephen Trent {BIO 5581382 <GO>}

Hi. Good morning, everybody. And thanks for taking my questions.

A - Frederico Curado {BIO 2004589 <GO>}

Good morning, Steve.

Q - Stephen Trent {BIO 5581382 <GO>}

Morning, Freddie. Just curious, I was wondering if you could give us a little bit of color on what was going on with this labor lawsuit, where there was -- you're already paying a settlement?

A - Frederico Curado {BIO 2004589 <GO>}

(multiple speakers), Luciano?

A - Luciano Froes {BIO 17907241 <GO>}

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Yes, I can do this. Actually, this is not a -- it's not a settlement. This is just a provision that we made. And we would have to go back to the '90s. This is prior to privatization. There was some labor reduction, preparing the Company for privatization. And some other things, entering some challenging process. And we are working on this. And the decision to make the provision is based on the opinion, on the legal that support us on this, that said that will be good, how we should do.

So that's a provision, it's not a settlement. They're still discussion. And there's some -- so, still waiting for that. It's not a final settlement.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Great. And just two other quick questions, if I may. And I share a congrats on the United order. I'm curious, when I actually take the valuation at firm value, at list price that you guys mentioned. And divide by the number of planes. And I do the same exact thing with the Republic order, I actually get kind of a moderately lower implied list price with United than I do on Republic. Is this just simple rounding, or are you making an effort to adjust list?

A - Frederico Curado {BIO 2004589 <GO>}

Steve, my sincere answer to your question is, I don't know. I have to check. Of course, as everybody else in the industry, we just informed (inaudible) aircraft (inaudible) list prices. So I don't know. I didn't even notice that. So thank you for the input. We will get -- if you agree, we will get back to you.

Q - Stephen Trent {BIO 5581382 <GO>}

Not a problem, Freddie, not a problem. And just one last thing, as you look at potential, ongoing potential order flow from the US market. And you have guys like American and United, that is, they're getting larger planes, are also getting rid of their 50-seaters. While American, it's clear what's occurring, how do you see United Airlines or customers like United progressing in terms of getting rid of their 50-seaters. And the guarantees that you have on those aircraft?

A - Frederico Curado {BIO 2004589 <GO>}

Well, I think the wave of bankruptcies seems to be over. I mean all majors, without exception, have gone through consolidation, have gone through bankruptcy. All the aircraft that had to be returned under bankruptcy have been returned -- for the industry, I'm talking about.

So I -- and let's keep in mind that the bulk of the existing 50-seaters fleet was delivered between late '90s, first half of the 2000s. So if you take up 12 to 15 year financing, it's -- we can see a gradual dilution, a substitution of those old aircraft by the new 70, 75-seaters being contracted right now.

So we believe there will be a, let's say, an organized way out of those aircraft, which we'll seek whoever is holding those equities. So we'll see secondary markets in Africas, Latin

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America, Eastern Europe. So a lot has been done, has been digested already by the industry, with the bankruptcy of the last 5, 6, eight years.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay, appreciate that, Fred. Let me leave it at that. Thanks for the time.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

Operator

Our next question comes from Myles Walton of Deutsche Bank. Please go ahead.

Q - Amit Mehrotra {BIO 15408970 <GO>}

Thanks. Good morning. It's Amit Mehrotra here for Myles. Just wanted to ask one quick question on the services revenue. Can you just provide us what the service revenue level was in the quarter?

A - Luciano Froes {BIO 17907241 <GO>}

Yes, hi, Amit. This is Luciano. Services was around \$195 million for total, considering all the business units.

Q - Amit Mehrotra {BIO 15408970 <GO>}

Okay. Okay, thanks. And then just one follow up on the EBIT margin in the quarter. Even if, after adjusting for the non-recurring items in the stimulus, it was still well below the full-year target. So I'm just wondering, in addition to mix, is there also some big step-up in stimulus benefit sequentially that drives the improvement? Can you just walk us through that a little bit?

A - Luciano Froes {BIO 17907241 <GO>}

Okay, Amit. So, yes, in line with what we mentioned previously, the stimulus should add up to about \$100 million for the year. Of course, you have to generate the revenues to start seeing that flow primarily in the COGS. So as we deliver more aircraft, we should see a step up in the stimulus benefits. And then, of course, in addition to the operating leverage and growth in revenues, etc., to meet the guidance, should bring us more at par with the figures that we've indicated.

Q - Amit Mehrotra {BIO 15408970 <GO>}

Okay. Okay, thanks. And just one last one, on the Defense business. The KC-390, can you just give us what the revenue contribution was in the quarter on that business. And maybe what we should expect as total revenue this year. And maybe what the slope of that business could be over the next couple years? Thanks.

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A - Frederico Curado {BIO 2004589 <GO>}

Yes, we don't particularly break down revenues per contract. Let's say the revenues in Brazil, taking all the contracts in Brazil, in the KC-390, the main contract that we have in Brazil, it's probably transitioning from some, let's say, 50% to 70% of our total revenues.

So, if you consider something in that ballpark, about 60%, 70% of revenues to Brazilian market. And KC-390 being the major contract there, you won't see -- (inaudible). Yes, for the year, for the year. Some 450 -- Luciano is just adding, some \$450 million for the year. That is our expectation.

Q - Amit Mehrotra {BIO 15408970 <GO>}

Okay. Great. Thanks so much.

Operator

Our next question comes from Darryl Genovesi at UBS. Please go ahead.

Q - Darryl Genovesi {BIO 20862546 <GO>}

Good morning, guys.

A - Frederico Curado {BIO 2004589 <GO>}

Good morning.

Q - Darryl Genovesi {BIO 20862546 <GO>}

So, can you just comment on what you're seeing on Business Jet pricing, particularly at the high end? I know you said the (inaudible) 100s are tough. But when I just look at your growth rate on a unit basis for the last couple quarters relative to last year, it would seem to me that you should be seeing kind of high 20-ish% kind of growth rate there. And what you're actually seeing is sort of mid-teens growth. So I'm just wondering if you're really seeing that big of a pricing hit, particularly at the top end?

A - Frederico Curado {BIO 2004589 <GO>}

Well, we're not seeing -- certainly not seeing a ramp up in prices. But we're not seeing, let's say, a stronger pressure than we had before. I think it has at least flattened out. And some more discipline in the production rates. So in a certain way, we kind of welcome what Cessna mentioned about maybe reducing their wide tail production. So that's -- that discipline will certainly bring a perspective of better margin to everybody.

But I would not say that as -- in the whole business, we are seeing a material upside as far as pricing. We are just about where we were. But it's not getting worse, at least. I think if it is moving, it's moving a little bit up. But not moving the new yet, not for us.

Q - Darryl Genovesi {BIO 20862546 <GO>}

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Okay. And then, I guess just the other question I had, just in terms of the stimulus, can you just give some color on sort of how you expect that to play out, when does it go away. And is it a cliff, or does it sort of kind of step down a little at a time, the way it sort of scaled up last year, assuming that that's not extended?

A - Jose Filippo {BIO 1726218 <GO>}

We expect -- we had in the First Quarter \$18 million in this impact. So we keep the -- what we indicated for the year, about the \$100 million --

Q - Darryl Genovesi {BIO 20862546 <GO>}

Right. I guess I was asking more about 2014.

A - Jose Filippo {BIO 1726218 <GO>}

The 2014 -- still, some of this, the payroll impact is for two years. So still keeping that. They may be renewed. But we don't have that, anything formal for that.

Q - Darryl Genovesi {BIO 20862546 <GO>}

So would that -- I mean, would that take you, kind of the Second Quarter of 2014? Because I think you started to see the benefit initially in kind of the Second Quarter of 2012?

A - Frederico Curado {BIO 2004589 <GO>}

No. What Filippo is trying to say is that this benefit -- which actually is a tax, is a change in tax. It's valid, at least, until the end of 2014. So we're going to see in 2014 what we will see in 2013, in that sense.

Beyond 2014. And that's why we do not have any firm indication yet.

Q - Darryl Genovesi {BIO 20862546 <GO>}

Okay, thank you.

Operator

Our next question comes from (inaudible) of TIAA. Please go ahead.

Q - Unidentified Participant

Hi. Regarding the delay in your deliveries this quarter, you had mentioned it was due to some financing issues at your customers. Can you please just confirm that those issues have been resolved. And that the deliveries are either -- that already delivered in Second Quarter, or set to definitely be delivered?

A - Frederico Curado {BIO 2004589 <GO>}

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Yes, pretty much so, pretty much so. You know, those are, of course, they are point issues. Either they have been delivered, will be delivered this quarter, if not all. But the majority of the aircraft. So we should see a step up in deliveries to both Commercial and Executive Jets in the Second Quarter.

Q - Unidentified Participant

Okay, thank you.

Operator

Our next question is a follow up from Pete Skibitski of Drexel Hamilton. Please go ahead.

Q - Peter Skibitski {BIO 6760095 <GO>}

Yes, Frederico, are you still on track to deliver the first Legacy 650 from China in the Fourth Quarter? And I just wonder if you expect the economics of those 650s to meaningfully differ from the Brazil delivered 650s?

A - Frederico Curado {BIO 2004589 <GO>}

Yes, we are, we are on track. And actually, as a matter of fact, I was there just last week. And the aircraft was already on the assembly line. And you know, it will depend -- it will depend on the rate of production. So if we stay in the lower range of 3 or 4 aircraft a year, probably going to have, probably a little bit less margin than when we have here in Brazil. If you go up to a high range of 6 to 9 to 10 aircraft a year, I would say very comparable. This is based on our history of the 145 in (inaudible).

Q - Peter Skibitski {BIO 6760095 <GO>}

Got it. Very helpful, I appreciate that. And last one, can you talk about the delivery ramp on the Legacy 500? I think you touched on this earlier. But I stepped off on the call. It sounds like you're on track to deliver the 500, I guess, in the middle of 2014. I'm wondering, should we think about kind of single digit deliveries next year, or is there opportunity for more than that? I was looking for some color.

A - Frederico Curado {BIO 2004589 <GO>}

Well, I'll give you very faint color. I cannot, of course, make much more precise comments on that yet. But probably, I would say, a low double digit -- again, beyond 10 aircraft is probably -- we would be looking at least in the low double digit 10-plus, 12, whatever, on 2014. And ramping up according to our backlog.

So it won't be just single digit. It will be more than that.

Q - Peter Skibitski {BIO 6760095 <GO>}

Okay. Great. Thanks very much.

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Operator

Our next question is follow up from Cai Von Rumohr of Cowan & Company. Please go ahead.

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

Yes. You had an abnormally low tax rate in the First Quarter. I know this is a difficult question. But could you give us a range on the tax rate for the year, barring any major FX fluctuations?

A - Jose Filippo {BIO 1726218 <GO>}

Well, what we have is that we didn't have any major effect of exchange rate in the First Quarter. So, we don't expect to see fluctuations so far. But as you know, this is something that impacts the way you calculate, because of, have the dollar as our function of currency. And the tax rate is calculated based on the reais figures.

So we don't -- we -- the number you have to consider, maybe, the standard of 25% as the income tax that we use for projection. It could be used -- like 25% would be enough now.

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

But you never really get to 25%. I mean, is a range of 15% to 20% -- give me a realistic range. If assumed, obviously, that the FX is relatively stable from here on out.

A - Jose Filippo {BIO 1726218 <GO>}

Yes, that's really the number that we should consider. There's some treatment sometimes that you go to the current income tax and the deferred income tax. But they all tend to put together in a 25%, if you take the full year.

A - Frederico Curado {BIO 2004589 <GO>}

Hi. We did have years where we had extremely high tax ratio, totally artificial, non-cash. So it's -- I appreciate -- you know, let's say, your difficulty is the same as ours. We have the same trouble here giving predictions to ourselves, to our Board. It's just this -- two different systems, one accounting, one to calculate tax based on reais. It makes it virtually impossible for us to make a prediction.

So I think -- will try to give you the best guess that we have. But it may really be all over the place, depending on the -- on how the (inaudible) FX develops.

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

Thank you, very much.

Operator

Our next question comes from Stephen Trent of Citi. Please go ahead.

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Q - Stephen Trent {BIO 5581382 <GO>}

Hello. Thanks, guys. Sorry about the follow up. I was wondering if you could tell us approximately what FX is something you're using for 2013.

A - Frederico Curado {BIO 2004589 <GO>}

Welcome, back, Steve. I think it's 2, right, Filippo?

A - Jose Filippo {BIO 1726218 <GO>}

Yes. It's 2 reais per dollar, for the full year. We're going for the -- flat for the year.

Q - Stephen Trent {BIO 5581382 <GO>}

Great. Thanks. And I also didn't hear your response on -- for the First Quarter, what was the level of service revenue you mentioned?

A - Luciano Froes {BIO 17907241 <GO>}

\$195 million, approximately --

A - Frederico Curado {BIO 2004589 <GO>}

\$200 million.

Q - Stephen Trent {BIO 5581382 <GO>}

\$200 million. Perfect. Thanks very much.

A - Frederico Curado {BIO 2004589 <GO>}

Thank you.

Operator

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

A - Frederico Curado {BIO 2004589 <GO>}

Just to thank you all for the participation. Look forward to talking to you next quarter. Take care. And bye. Have a nice week.

Operator

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

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