Q1 2019 Earnings Call

Company Participants

- Paulo Kakinoff, Chief Executive Officer
- Richard Freeman Lark, Executive Vice President, Chief Financial Officer and Investor Relations Officer

Other Participants

- Barbara Halberstadt, Analyst
- Daniel McKenzie, Analyst
- Duane Pfennigwerth, Analyst
- Joshua Milberg, Analyst
- Petr Grishchenko, Analyst
- Richard Lark, Chief Financial Officer
- Savi Syth, Analyst
- Stephen Trent, Analyst
- Unidentified Participant

Presentation

Operator

Good day, and welcome to the GOL Airlines First Quarter 2019 Results Conference Call. This call is being recorded and all participants will be in a listen-only mode during the Company's presentation. After GOL's remarks, there will be a question-and-answer session, at that time further instructions will be given. (Operator Instructions) This event is also being broadcast live via webcast and maybe accessed through the GOL website at www.voegol.com.br/ir and the MZiQ platform at www.mziq.com. Those following the presentation via the webcast may post your questions on the platform and their questions will either be answered by the management during this call or by GOL Investor Relations team after the conference is finished.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of GOL's management and our information currently available to the Company. They involve risks and uncertainties because they relate to future events and therefore depend on circumstances that may or may not occur. Investors and analysts should understand that events related to micro economic conditions, industry and other factors could also cause results to differ materially from those expressed in such forward-looking statements.

At this time, I would like to hand the call over to Paulo Kakinoff. Please go ahead.

Paulo Kakinoff {BIO 5160310 <GO>}

Good morning, ladies and gentlemen, and welcome to GoL Airlines conference call. I am Paulo Kakinoff, Chief Executive Officer, and I'm joined by joined by Richard Lark, our Chief Financial Officer.

Richard Lark {BIO 3484643 <GO>}

Good morning. Good to be with you today.

Paulo Kakinoff {BIO 5160310 <GO>}

This morning, we released our first quarter figures. Also, we made available on GOL's Investor Relations website three videos with the results presentation, financial review and brief Q&A.

We improved our operating indicators. In the quarter, GOL's RPKs increased by 6.4% from BRL10 billion in 2018 to BRL10.6 billion this quarter, driven by a 7% increase in the number of transported passengers. Increased demand allowed GOL to optimize yields through dynamic revenue management. Average yield per passenger increased by 1.9% quarter-over-quarter reaching BRL0.286. Supply increased 5% driven by a 3.2% increase in seats and increasing the average stage length. This indicator includes the impact of the grounding of seven MAX 8 on March 11. The average load factor was 81.5%, an increase of 1.1 percentage point compared to the same period in 2018. We continue to drive strong revenue growth. The combination of higher demand and optimized pricing resulted in net revenue of BRL3.2 billion, an increase of 8.3%.

Net RASK was BRL0.246, an increase of 3.2%. Net PRASK increase increased 3.3% reaching BRL0.233. Average fares increased by 1.3% from BRL335 to BRL339.

GOL's 2019 guidance is for net revenues of approximately BRL13 billion. GOL's current network serves higher yields routes and is the leader domestic market with a market share of 36%. The Company is also a leader in the corporate customer segment with the largest market share of business traffic in Brazil.

Regarding the temporary grounding of MAX 8 aircraft, we emphasize that since the beginning of the operations with the MAX 8 in June 2018, we have operated nearly 3,000 flights totaling over 12,700 hours, offering absolute safety for our customers. Boeing is executing a comprehensive and more disciplinary strategy for the MAX 8 update and soon our customers will be able to benefit again from all the technology and comfort offered by these modern aircraft. Since March 11th, the Company's operating flights from our international hubs in Brasilia and Fortaleza to the United States, with 737-NG aircraft.

With that, I'm going to hand you over to Rick, who is going to take us through some additional highlights.

Richard Freeman Lark {BIO 3484643 <GO>}

Thanks, Kaki. First, we would like to comment about GOL's cost environment. Total CASK ex non-recurring in the first quarter was BRL0.204, 4.7% higher. CASK ex-fuel excluding non-recurring increased 3.2%, mainly due to the 16.2% appreciation of the US dollar against the Brazilian real, the end of the payroll tax relief program, higher depreciation due to higher capitalized maintenance on aircraft components including engines, and a fleet increase of seven new aircraft, four net, in addition to higher passenger expenses resulted from the grounding of the MAX-8 fleet.

GOL remains the cost leader in South America for the 18th consecutive year. Our margins remain solid, the combination of better pricing, higher demand and execution of the fleet renewal plan permitted GOL's recurring operating income to reach BRL546 million, with recurring EBIT margin of 17% in the first quarter of 2019. Recurring EBITDA was BRL952 million and recurring EBITDA margin reached nearly 30%. GOL's 2019 guidance is for an EBITDA margin of approximately 28%.

The second point to highlight is our cash flow management. The combination of our operating cash flow generation of BRL254 million in the period and higher cash liquidity improved the Company's financial flexibility. Total liquidity including cash, financial investments, restricted cash and accounts receivable, was BRL3.5 billion at March 31, 2019.

Lastly, we would like to share the continued success of GOL's liability management. The net debt excluding perpetual bonds to the last 12 months EBITDA ratio was 3.3 times at the end of March 2019. We continue focused on the improvement of our capital structure including the amortization of BRL148 million of the Company's seventh issuance of debentures and the tender offer for 15% of the 2022 Senior Notes.

We also carried out an innovative issuance of exchangeable senior notes totaling $300 million in the quarter convertible into GOL shares at an 85% premium over the stock price on the date of issuance. This issuance bears an interest rate of 3.75% per year, reducing GOL's average cost of debt by 50 basis points. These transactions represented additional deleveraging of the balance sheet and even better matching of operating cash flow generation with amortization of liabilities. The liability management reduced the Company's cost of debt and improved its credit metrics. Currently, the average interest rate is 7.7% for local currency debt, and for dollar-denominated debt, the average interest rate is now at 6.3% compared to 6.8% in the fourth quarter of 2018.

GOL has maintained its commitment to financial discipline, managing the effects of Brazilian currency through its efficient capacity management and dynamic yield management. For 2019, we expect GOL's domestic capacity growth to be between 3% to 4% and international to be between 35% to 40%. Non-fuel CASK is expected to be around BRL0.14. We have projected EBITDA and EBIT margins in 2019 at around 28% and 18%, respectively. Leverage measured as net debt excluding perpetual debt over EBITDA for 2019 should be 2.9 times, reflecting our commitment to reduce leverage on the Company's balance sheet.

Now, I'd like to return to Kakinoff.

Paulo Kakinoff {BIO 5160310 <GO>}

Thanks, Rich. In summary, we worked hard to maximize our results this quarter. Our commitment to continuous improvement in results has proven the strategy assertiveness of offering a differentiated and high-quality product while relentlessly focusing on cost efficiency. We remain focused in offering the best experience in air transportation. We have exclusively services to customers on new and modern aircraft that connect our main markets with the most convenient schedules. We are committed to a highly-disciplined capacity management and prudent management of the balance sheet and liquidity, maintaining cost leadership and continuing as the preferred airline for customers, while driving sustainable margins and returns for shareholders. And to conclude, we are optimistic for 2019 with the continuous improvement of the Brazilian economy and the aviation sector in the country.

Now, I would like to initiate the Q&A session.

Questions And Answers

Operator

We will now begin the question-and-answer session. (Operator Instructions) And our first question today comes from Duane Pfennigwerth with Evercore ISI. Please go ahead with your question.

Q - Duane Pfennigwerth {BIO 7329167 <GO>}

Hi, thanks. Rich or Kakinoff, can you update us on the auction process for Avianca Brazil? What that looks like as of today is May 7th still a good day and any thoughts on what you're actually going to be bidding on?

A - Paulo Kakinoff {BIO 5160310 <GO>}

Hi, Duane. Good morning. Actually what we know is pretty much the official figures. The auction is scheduled to happen by Tuesday next week and we are now noticing that Avianca has performed flights at four different airports and they had been able to actually keep the company operating with the current six -- five to six planes that they have available. GOL is committed to this auction as previously informed. So we are supposed to offer a minimum (inaudible) for at least one of the UPI. So this is why we got so far.

Q - Duane Pfennigwerth {BIO 7329167 <GO>}

Thank you. And maybe more detail than you're willing to get into, but can you speak to what the UPI that you're interested in covers? Is it a specific part of their network or is it sort of a blind allotment divided by six?

A - Paulo Kakinoff {BIO 5160310 <GO>}

Yes, I think you are right. We wouldn't like to give any kind of disclosure at this moment because that's part of our strategy to the auction. And this is an auction for real and not seen artificially built to determine one single winner. Therefore, we are participating in this auction as we would in any other normal auction. And we cannot, due to this situation, give you any kind of disclosure, which could jeopardize our strategy to that date. Okay?

Q - Duane Pfennigwerth {BIO 7329167 <GO>}

Thanks. And then just just for my follow up, maybe Rich, as you think about the June quarter what you're seeing in demand and bookings trends and as we think about comping the trucker strike last year, any any color you could provide into the June quarter on the revenue environment would be appreciated.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes, sure you're right. Remembering last year in mid-May, we had a collapse of the demand curve because of a nationwide trucking strike, which hurts the year-over-year comps in -- the way I would characterize that, we're seeing very strong bookings and that's also reflecting in yields and we expect to see something on the order of 15% year-over-year increase in the revenues for the second quarter (inaudible) volume effect and the yield effect in there; a big chunk of that is coming out of the yield side of the equation, because load factors are at peak levels. So that's what we're kind of seeing at this point. And that's also what motivated us to upgrade our guidance for the year for about BRL100 million from the BRL12.9 billion to the BRL13 billion.

Q - Duane Pfennigwerth {BIO 7329167 <GO>}

Okay. Thank you.

A - Richard Freeman Lark {BIO 3484643 <GO>}

You're welcome.

Operator

And our next question comes from Dan McKenzie with Buckingham Research. Please go ahead with your question.

Q - Daniel McKenzie {BIO 15071178 <GO>}

Hi, thanks. Good morning, guys. A couple of questions here. On the revised outlook, just a couple of clarifying questions. Does the revenue in growth outlook include upside from Avianca Brazil's assets at this point and/or the structural reorganization of Smiles?

A - Richard Freeman Lark {BIO 3484643 <GO>}

Hi, Dan. No, nothing from a potential acquisition, specifically, meaning, nothing from us increasing our assets. But overall, in terms of the market, we are now with the more definitive nature of that situation, the company has basically -- significantly wound down over the past couple of weeks. So that component where Avianca Brasil had the largest overlap with GOL's operations, that component is in our forecast, for sure. So a part of that is in the forecast and in the other component really relates to the sourcing and overall demand. And on the -- in terms of the Smiles Incorporation now, as you saw in our guidance, the budget for the minority interest is still outstanding in our 2019 guidance, it's still being excluded from bottom line net income.

Q - Daniel McKenzie {BIO 15071178 <GO>}

Yes. Understood. And then, so I guess just a couple more questions here. First, just the MAX grounding. How are you thinking about the impact to the full-year cost just given the revised CASK ex-fuel forecast? And then just tied to the last question here, your comment about Avianca, just curious to what extent there was revenue pressure in the first quarter tied to Avianca perhaps pricing for cash?

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes, I'll do those questions, Dan. Right now, based on what we know now with the MAX, there would be an impact of around BRL40 million in our forecast for this year. That's up to today, meaning, with what we've done currently with the grounding and assuming that Boeing's forecasts bear fruit, which is during the month of May they will be then the MAX grounding and then MAXs would be flying again in the second half of the year. In our first quarter numbers, we had around BRL10 million of costs that related to the MAX grounding, specifically.

And your second question as well I think is relevant. We did see in the month of March was some very intense price discounting coming out of Avianca as they were in that specific mode. And so that impacted yields negatively in the quarter because of the March -- in fact January, February was actually pretty solid. And then in March, we saw that effect and also remembering that company operates in the main show [ph] markets with a big overlap with us and so we were seeing a bit of that especially in the last 15 days of March, in the first 15 days of April.

Q - Daniel McKenzie {BIO 15071178 <GO>}

Perfect. Thanks guys.

Operator

And our next question comes from Savi Syth with Raymond James. Please go ahead with your question.

Q - Savi Syth {BIO 17476219 <GO>}

Hi, good afternoon. Just on the -- just to follow up on on the kind of MAX grounding, just wondering if this does last into kind of the winter holiday season, what optionality you have if you look at the kind of US airlines, they seem to imply during peak season having kind of a bigger percentage impact than their fleets would imply and just kind of wondering if maybe GOL has some more flexibility to kind of limit that impact if this does go into the peak demand period?

A - Paulo Kakinoff {BIO 5160310 <GO>}

Hi, Savi, this is Kakinoff here. Yes, we could have an additional impact, but that is in comparison to any other airline -- a major airline in the world suffering by the 737 MAX grounding much lower. This is because we were operating only one route that was exclusively operated by 737 MAX, which was -- that was at this stage. Now, we are performing the same route with the NG. We have one stop over Dominican Republic for refueling and that would be the single route basically affected by by not having the 737 available in July, which is the Brazilian high season. We can redesign our network in July to further reduce lower profitable routes and and reallocate some of our NGs to compensate the lack of 737 MAX with towards more demanding/profitable routes than we would normally do. So basically, we could re-accommodate it, possibly have an additional impact than we are receiving today, but nothing that it would dramatically change the July's result.

Q - Savi Syth {BIO 17476219 <GO>}

Understood. That's helpful --

A - Richard Freeman Lark {BIO 3484643 <GO>}

I would just -- Savi, I would just add to that. In terms of the fleet plan and what we have currently in terms of the flexibility that you are asking the eight MAXs that we had in the fleet plan, seven from last year and that we grounded and then the additional one we would have already received this year, those are fully covered by NGs, which there was four NGs that we are not returning. And so they're not going out of the fleet this year based on that. And then also four NGs where we re-calendarized the maintenance schedule. So within the existing fleet, we're able to source capacity from eight NGs that were either going out or going to be grounded for maintenance to cover those eight MAXs currently that are not flying.

And then as of July, now we start to receive roughly one to two aircraft per month off the MAX order. So in the plan A we're receiving those aircraft as Kakinoff say, to the extent that we're not receiving those aircraft as of July, we would then have to make some further adjustments in the fleet plan. So think about it, and those two parts, the first part which is the current MAXs that we have, they've already been covered by the flexibility we have with the NGs. And second part would be the future MAXs to be delivered, which start in July, we would then have to cover those with alternative measures.

A - Paulo Kakinoff {BIO 5160310 <GO>}

So Savi, just to -- the topic, in parallel, we could also get access to temporary leasing contracts in order to fulfill an expected high demand to be present in the market over the following two to three months. So I think, we are also restructuring ourselves to get access to some temporary leasing contracts, which could not necessarily to compensate the MAX effect but if we continue to see the current demand, which is pretty high we could also afford to get four, five, six additional planes for temporary contracts, such as one year or a year and a half which would also make us able to absorb a more benign market than we had forecasted before and it's pretty much comparable to what we are seeing exactly today. So I mean our demand is pretty high and we can have that additional resource in place.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes. We're preparing for this excess-benign [ph] scenario effect. As you know, coincidentally, simultaneously with all this, we have a situation of Jet in India and that has resulted in the availability of NGs, which are the exact aircraft that we fly. So were -- we have that as a potential source of some short-term leases for NGs if we need them to cover any delays in MAX deliveries in the second half of this year which is possible.

A - Paulo Kakinoff {BIO 5160310 <GO>}

And even if the MAX is back and the market we will continue to be as strong as it is today, we could have on top of the MAX being back to the game by the end of May beginning of June, we could also decide upon bringing some additional planes to compensate this additional demand.

Q - Savi Syth {BIO 17476219 <GO>}

And I think that answers my follow up, but just to clarify. So if you do get these kind of the Avianca Brazil routes, is that kind of how you would plan to address additional flying that you will have and is that reflected in the guidance or not?

A - Paulo Kakinoff {BIO 5160310 <GO>}

No. I think that there are too -- at the moment, you have too many moving parts and I think that the good assets or the positive side is that all those moving parts are positively suppose to deliver additional demand, additional results. And from the current landscape, I think that the alternatives only positive to the scenario that you had previously (inaudible). Avianca might be another positive layer on top of everything that had discussed right now. But we are not considering all those things and definitely they are not reflected completely into our current guidance.

Q - Savi Syth {BIO 17476219 <GO>}

All right. Very helpful. Thank you.

Operator

And our next question comes from Stephen Trent with Citi. Please go ahead with your question.

Q - Stephen Trent {BIO 5581382 <GO>}

Good morning, gentlemen, and thanks very much for taking my questions. I actually just had one or two follow-ups to what Savi and some of the other guys have asked. But first off when we think about the Avianca Brazil slots, have you guys heard any credible interest from any foreign carrier and even looking at those slots as it maybe naively kind of seems to me, it's too smaller footprint that it being encircled by three big domestic airlines. But any credible foreign interests that you've heard of by chance?

A - Paulo Kakinoff {BIO 5160310 <GO>}

We have heard -- hi, good morning. Actually, we have heard some, I would say, curious things hanging from the Uber, who would be interested in it up to a new entrepreneur from...

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes, when we heard a couple of days ago that Uber was...

A - Paulo Kakinoff {BIO 5160310 <GO>}

Yes, yes, Uber. So these sets of (inaudible) that there are several speculations, but nothing -- up to now, nothing material, nothing concrete.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Very helpful. That's pretty amazing. I was also just wondering when we think about these recent announcements with regulations, I mean, one kind of reducing the state taxation on jet fuel kerosene, and two, this issue about checked bags. One, any color with respect to where else you might be able to expand with this jet fuel kerosene tax reduce, I think you mentioned Sao Paulo, and I'm not sure if you're able to give us any further detail. And on this checked bag, assuming it gets rolled back, I mean, isn't that just going to go into higher fares anyway?

A - Paulo Kakinoff {BIO 5160310 <GO>}

Hi, Steve. Actually, it's really hard to believe that the government would step back on the baggage shifting [ph] because that would be at least a kind of contradiction in comparison to what the Brazilian Seaview authorities have put in place so far in order to open up the Brazilian markets to be -- to have a regulatory structure quite comparable to the most developed markets in the world. And even this government has publicly said pretty liberal. So that movement coming from a quite punctual situation in the Congress, I don't think that will be accepted by the government. Honestly, I don't believe that the baggage fee will change, mainly because, as you know, the same government is pushing the same Congress very, very strongly to get the foreign capital lift been being approved. So those are two opposite decisions, I mean, to have the market open for foreign capital and at the same time stepping back with the baggage or the baggage fee or so. I guess that Richard would like also to --

A - Richard Freeman Lark {BIO 3484643 <GO>}

On the fuel -- yes, I mean, Sao Paulo was a pioneer in reducing the fuel tax and exchange for the airlines adding additional development, bringing passengers from other parts of Brazil into Sao Paulo, generate tourism and additional tax revenues for the state. The expectation is that other states will follow -- there's nothing specific that we see happening in the near term, but the expectation is that our conversations about some other states pursuing some similar development objectives with lowering of fuel taxes.

But Sao Paulo was the big nut obviously for the country and for us, we it's about 30% of our revenues, the flights in and out of Sao Paulo and previous to this initiative by the Sao Paulo state government had the highest jet fuel taxes, so we're actually doing tankering and other measures so that we're reducing our actual fuel consumption on the overall network down to about 23% percent of the total. And so for us the Sao Paulo piece was significant on its own merits. But I think, there are discussions that we could potentially see some other states follow with that type of initiative, but nothing specific at this point.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Let me leave it there. Very helpful. Thanks, guys.

Operator

And our next question comes from Michael Linenberg with Deutsche Bank. Please go ahead with your question.

Q - Unidentified Participant

Hi, guys. This is actually Matt on for Mike. A few questions on the warrant offering. What drove the decision to bring warrants to market? Could you give us a rundown on the mechanics of the transaction and how would you characterize the balance sheet benefit?

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes, I think Matt you're referring to the warrants offering that is being done this week, is that correct?

Q - Unidentified Participant

Yes.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes. That's only being done -- in the month of March, we issued a convertible bond, and in Brazil, preemptive rights are an obligation. And so we're doing that offering of warrants to basically satisfy the preemptive rights obligation. How it worked in the context of the convert is that the offshore company that issued the convertible bond is basically subscribing those warrants such that in the future if those investors who hold that bond want to convert into the underlying equity going through ADRs all the way down to the local PN shares, those shares will already be effectively issued through this warrant structure. And concurrent with that, we're also offering that warrants to any investor in our current shareholder base that would want to take up those preemptive rights on that warrant, but the motivation for that of the warrant specifically is not a capital raising, the capital raising was already done with the combination of the original issue and the green issue we raised, $345 million on the convertible bond, which -- which is convertible into GOL ADRs and then those ADRs through the warrant issue will also be fungible with an equivalent amount of shares in the local PN shares. So the reason for that warrant offering it's just kind of the last leg of the complex convertible bond offering that we did in March.

Q - Unidentified Participant

Thanks. And just as a--

A - Richard Freeman Lark {BIO 3484643 <GO>}

What was the second part of your question.

Q - Unidentified Participant

Just as a quick follow up, have you seen any share shift in Brazilian loyalty market? I know some of your competitors in the past have called out taking a bigger slice of the pie in the loyalty market.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Well, I would say a couple of factors there, because we have two competitors currently that have had a reduced focus LATAM just finished a couple of weeks ago, they are taking of Multiplus and obviously Avianca has -- with its restructuring has been on focus. That has provided an opportunity in the current market. There has been some market share shifts currently from those airline companies into our loyalty program. We've also seen Azul being more aggressive with their program and also the banks, because in addition to the airline programs, they also compete directly with many of the commercial banks here in Brazil. So on the volume side that's what kind of what we're seeing. On the margin side, we are seeing more competition on pricing across the board, especially as the airlines are starting to use the loyalty program more as a marketing tool as opposed to having an isolated business focused on maximizing the profitability of a standalone any. But I think we're -- it feels a bit like we're in a bit of an inflection point now.

Also generally, what we see is the two businesses -- the airline passenger business and the loyalty program business tend to be counter cyclical when you talk about margins, where kind of one year, three years or so now of our secular growth phase, where the demand from paying passengers increasing, and kind of the the opposite of that or if will, the one minus portion of that is the cost of goods sold of the loyalty program, and so we're bit of an inflection for right now, kind of transitioning from what the market has looked like over the last five or six years to what it will look like over the next five or six years. And we do expect that to be a frontier of increased competition, especially as the industry structure in Brazil consolidates and reformulates, and the airlines strategically are reformulating how they're using their loyalty businesses to drive loyalty and growth and compete, and so on.

Q - Unidentified Participant

Thanks for taking my questions.

Operator

And our next question comes from Barbara Halberstadt with Bank of America. Please go ahead.

Q - Barbara Halberstadt {BIO 18022271 <GO>}

Hi. Thanks for taking the question. I jumped in a little bit later. So I'm not sure if you already answer it, so my apologies. Just wanted to have an update on the Smiles corporate organization, if there is any deadline in the short-term to come up with a final structure. Just if you could give us some color on that, it would be great. Thank you.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Hi, Barbara. As we disclosed in December, we're in discussions with the special independent committee that was constituted by the Smiles Board, and as soon as we have any news from that negotiation, we both us as well as Smiles would be disclosing that to the market. But we don't have any news at this particular moment.

Q - Barbara Halberstadt {BIO 18022271 <GO>}

And now no deadline, I mean, it's no target end of the year or the next quarter?

A - Richard Freeman Lark {BIO 3484643 <GO>}

So there's no pressure on the independent committee in terms of the amount of time that they have to analyze the transaction, and we're currently in the middle of those discussions.

Q - Barbara Halberstadt {BIO 18022271 <GO>}

Okay, great. Thank you.

Operator

And our next question comes from Josh Milberg with Morgan Stanley. Please go ahead with your question.

Q - Joshua Milberg

Hi, everyone, thank you for the call. My first question relates to the big drop-off in your maintenance costs seen in the period, and I was just hoping you could comment on what drove the change in the capitalization level, and also what we could expect for this line going forward?

A - Richard Freeman Lark {BIO 3484643 <GO>}

No, I think part of that just relates to the shift in the fleet, Josh, there's no big drop-off per say, we did -- I'm trying to think specifically of what you're referring to there, but...

Q - Joshua Milberg

I'm referring to the referring your 60% decline year-over-year in your maintenance materials and repairs line.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes. Nothing specific. I can maybe get back to you offline on that and see that nothing specific. As you know we in 2016, '17 and '18 we're peak -- we're kind of peaking maintenance expenses for us as it relates to the engine overhauls. This year, we go into a transition towards a more normalized level where in two years we hope to be back down to around a BRL350 million to BRL400 million a year run rate from this roughly BRL600 million to BRL650 million run rate that we've been at as we've kind of peaked on the engine overhauls, and every time we do this engine hauls, we basically get seven years of useful life to the next maintenance event. Also, we have on a quarterly basis there can be variances based on what we're doing specifically is really to seasonality and so on. So I think in the quarter-over-quarter comparison, we did have some lower maintenance events in the first quarter related to our utilization and higher seasonality having less in maintenance. But nothing nothing specific that would be kind of a structural change other than just kind of this year we're shifting down to a lower level, but I'll take a look at that and see if there's anything else and I'll get back to you offline on it.

Q - Joshua Milberg

Okay, fair enough. And one thing you guys had highlighted in the release was a higher capitalization of rotables and components repairs.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Well, yes, we do capitalize a portion of the maintenance there that goes and then is basically depreciated over a five to seven-year period. There was a slight increase in that in the first quarter of this year based on the nature of the maintenance costs maybe about BRL30 million to BRL40 million of additional capitalization there that perhaps that's in the previous quarter, but I will just have to look in for the micro detail on that and I'll tell you if there's a better way to look at the apples-to-apples comparison.

Q - Joshua Milberg

Okay. Got it. Thanks for that. And then you already covered a lot of ground obviously on the MAX, but I was hoping you could just touch on the issue of potential compensation from Boeing for the grounding, if that's something on which you can say anything at this stage.

A - Paulo Kakinoff {BIO 5160310 <GO>}

All I can tell you that, we are -- we have this kind of situation predicted in our contract, we cannot give the disclosure on how specifically this would evolve but I can tell you that we have no major concerns regarding the necessity of having some kind of compensation being provided by Boeing.

Q - Joshua Milberg

Okay, Kakinoff. Thanks, Richard. Thanks to both of you.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Thank you.

Operator

And our next question comes from Petr Grishchenko with Barclays. Please go ahead with your question.

Q - Petr Grishchenko {BIO 19084897 <GO>}

Good afternoon and thanks for taking my questions. Some of those already answered, I guess I want to switch gears to your outlook for '19 and '20. I assume your guidance on fuel prices takes into account the fact that about what 60% of your fuel consumption is hedged at I think $60. So first, is this Brent or WTI? I'm just curious. And then, I'm looking at '20 and it seems like the cost is only marginally higher and there are no hedges, so I'm just wondering how to think about that?

A - Richard Freeman Lark {BIO 3484643 <GO>}

That's not the case. I mean, we're about 30% hedged for 2020 also in the low $60s, those are WTI prices. We generally go out two to three years and work on hedging. We just provided for reference there how much we have hedged for 2019, but if you look in our financial statements you can also see we have for 2020 we also have about 10% hedge in 2021. And basically how we do specifically at GOL hedging is taking advantage of the forward curve, backwardation and credit capacity to create value and putting on hedging well in advance. And so for example these hedges that we have now for this year 2019, we basically put them on in the middle of last year and then topped up a little bit in December when prices came down. But having said that, that fuel price per liter guidance we're giving you there is not a hedge price, that is a -- that's indicative of what we expect our price to be, primarily from the suppliers here in Brazil. We don't -- we're not forecasting gains or losses on hedges because that will depend on how that rolls forward on a quarterly basis. For example, the mark-to-market to day to day [ph] on our hedge positions is about BRL100 million, if we were to unwind all of those hedges and put the cash in the bank, we would have about a BRL100 million but we don't it that way. We will basically -- we will manage the positions if the volatilities get too far off course up or down and we'll also take advantage of the market as well as to manage our downside positions and buyback the puts in (inaudible). But basically that hedge position that's there, if for example things stay where they are from now to the end of the year, over the next three quarters, we would see -- for the end of December, we would realize around BRL100 million of gain if things stayed where they are stable. And that would be a slight reduction to our overall fuel expenses but that fuel price guidance in there, which was revised up a bit is is based on our forecasts here for oil prices and what we think the effective RASK priced us here locally is.

And that guidance we give there, which is probably some of the more detailed guidance you get out of any company maybe anywhere, is really just to help those who are projecting -- develop their own projections. I mean that that guidance is developed by a lot of questions that we get asked repeatedly and all the data we're providing there is pretty much everything that the market would need to estimate our results. It also allows us to be able to talk about results because if we wouldn't be providing this level of guidance, we'd be providing selective disclosure and individual conversations. And so there's a lot of reasons why we give that level of detail. It's not so that people can speculate against or bet against our internal estimates on oil prices or exchange rates. We do not want to get into that. So we're providing there how much we think we're going to be consuming and how much we're going to think we're going to be paying in terms of the price per liter on average. Obviously, there's a lot of volatility there are. We have a specific view on oil as well, but that's also so that analysts and investors, you can also kind of put in your own assumptions there on the fuel price if you want to do some simulations. So that I think that's kind of gives you a lot of information that kind of help you think about that in terms of how we're managing in.

Q - Petr Grishchenko {BIO 19084897 <GO>}

That's very helpful. Thank you, Richard. And another I wanted to follow up on your comments on the food [ph] commitments. I mean, given IFRS 16 implementation, I'm just curious in your thought process in evaluating operating versus finances and leases going forward, do you think it changes the math a little bit for you or not?

A - Richard Freeman Lark {BIO 3484643 <GO>}

Changing the math meaning what, the situation of the MAX?

Q - Petr Grishchenko {BIO 19084897 <GO>}

Well, given you evaluation whether you're going to enter operating or finance the leases for the new aircraft given the changes in the accounting.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Oh, no, I see, given the IFRS, the new accounting, no. No that doesn't change that. Our decision on how we finance the fleet as an economic decision and a risk management decision. In our first order with Boeing, we did 80 aircraft out of the factory, we did half and half, half the mortgage finance leases and half sale leasebacks; the philosophy there being, if you need to adjust your capacity, it's a little bit easier to adjust your operating lease capacity than your finance lease capacity, if you need to adjust up or down quicker. Having said that in this -- in our next cycle, which is our second order with Boeing, our plan is to do 60% mortgage finance leases and 40% sale leaseback over the next eight years or so. Our economics are better as a company on the finance leasing mechanism, because the costs there are lower, but that's traded off against the flexibility component with having operating leases, which allows us to kind of upsize and downsize quicker than the finance lease.

Going forward, I mean, our 2018, 2019 and most of our 2020 deliveries have already been done in the sale leaseback format. Starting in 2021, 2022, 2023, we will be focusing more on a finance lease format, which will be divided among a variety of export credit facilities and other things, which we're working on now, and I expect end of this year, beginning of next year, we'll be announcing -- we'll give you some more visibility on what we're doing on the finance lease component. But it's not driven by the accounting. All -- obviously, all the aircraft today are treating as a finance lease, with whether it is an operating lease or finance lease. I mean, effectively go in there at the real economic cost of those leases. That's what you're seeing on the balance sheet today in terms of debt, as well as the interest expense. That's a more accurate representation of what our actual leverage is and our actual financing costs. I do expect though over the next couple of quarters, it's going to be interesting for us, interesting for me to see it kind of how the market reevaluates benchmarking and companies and GOL, as well, because it does change a little bit, how the operating leverage and the financial leverage is presented. And so it's going to be interesting to me to see how that evolves and how the market looks at that. If you haven't already -- if you have some time later in the third video that we've posted on the site this morning, the Q&A video in the first part of that, we put to two benchmarking slides in there, which you're looking at the 2018 data. But we put two benchmarking slides in there, GOL versus the global peers on the Latin peers, that gap, that is going to tend to I think magnify going forward, meaning given that GOL is a high efficiency airline with a high value product that will start to show a little bit more clearly in the accounting now, which is a separate issue than what you were asking, but obviously given that our biggest asset is the fleet and our primary liability, if not our only liability is secured and unsecured financing related to the aircraft acquisition that we do at the holding company level. It has various interesting implications for how you look at asset turnover, profitability, as well as leverage, and some people do look at airlines like they look at the (inaudible) and things like that.

So the new accounting tends to make us look a little bit more attractive on a return on capital and return on equity perspective than the old accounting did. And so just to kind of, plus airline nerds who like to look at this stuff it's going to be I think more interesting over the next couple of quarters, but see how we kind of dialogue about this.

Q - Petr Grishchenko {BIO 19084897 <GO>}

Great. Thanks a lot. Very helpful and best of luck to you guys.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Thanks, Petr.

Operator

(Operator Instructions) And our next question is a follow up from Savi Syth with Raymond James. Please go ahead. Ms. Syth, your line is open.

Q - Savi Syth {BIO 17476219 <GO>}

Hi, sorry about that. I have this on mute. I just have a three-part question on non-recurring expenses. Just first, what was in 1Q? Two, were there any kind of gains on sales and kind of what do we assume not much the rest of the year given the kind of the MAX situation? And then the third one, a little bit of a I'm guessing you might not be able to answer too well, but with Avianca Brazil, if you do kind of get any of those assets, should we kind of think of some non-recurring expenses related to any ticket sold that you might be taking responsibility for and how should we think about that impact? Thanks.

A - Richard Freeman Lark {BIO 3484643 <GO>}

Yes. That's a future question right? Well, there's an answer to that. But on your first question, we've just been providing information on the non-recurring, you guys can use whatever date you want, we're just giving the data so you can get a good estimate of what the underlying operating profitability is and then what the other costs are, as we have been doing this major fleet renewal. In the first quarter, we had around BRL40 million of non-recurring expenses, about BRL20 million -- about half that amount was related to the return of one aircraft return, we basically returned one aircraft in the quarter and had some other expenses related to a second aircraft that is almost ready to be returned, an NG aircraft. We had around BRL10 million of expenses related to reaccommodation, food and some other costs related to the grounding of the MAX aircraft we did. And there's about BRL10 million of other expenses. There we did an offering in the Q1 of fundraising where we had some additional expenses. That's pretty granular detail, it's not a big number. There was this BRL40 million that we just pulled out of that to give you a better visibility on that.

There's no significant NG sales plan currently. That was our plan starting the year. We accelerated many of our 2019 expectations on NG sales into those 13 aircraft that we sold in the fourth quarter of last year. And so we started this year not planning to have any major NG sales programs unless we were to get an opportunity. So this is before the MAX grounding. I was having said that you know currently where we are right now, we are delaying the re-deliveries of four NGs and we've recalendarized the maintenance of four NGs this year. So that's actually going to have an economic positive effect for us because, we generally can spend as much as $2 million for every NG that we have to return out of the fleet. So we're not going to be having those expenses this year. And we're also going to see potentially some slightly lower maintenance expenses in the second half as we recalendarize the maintenance on those NGs, those eight NGs that we're going to have flying as opposed to either going out of the fleet or in maintenance.

On the MAX deliveries this year, those were done in the sale leaseback format and so those aircraft, anytime we do those kind of sale leasebacks, they have a small gain. So we haven't really -- we received one MAX this year. And so we have no sale leaseback gains on the received MAXs to the extent we have the schedule normalize in the second half of the year and we're receiving those MAXs off of our Boeing order under sale leasebacks, we would recognize some gains related to that. But that is not in our forecast at this point in time.

And then on your final question, the the way that the restructuring plan was approved for Avianca Brazil in the (inaudible) the document that the creditors approved; if we acquire one of the UPIs, we would assume a commitment for up to $20 million of air traffic liability, which would be our maximum assumption of any type of liability there, because these are isolated productive units which means their bankruptcy remote. And so as you know the way the air traffic liability works, it's -- it can be absorbed into your existing operations, on your existing capacity with a small marginal cost. And currently Avianca Brazil's operations are significantly reduced and have wound down substantially and we have already been over the last four weeks or so together with the other airlines in Brazil as part of what we normally do transporting Avianca passenger -- I think to date we probably transport about 13,000, 14,000 passengers of Avianca; it's already kind of chipping away into the air traffic liability that they have there. But the answer would be a maximum liability of $20 million if we were to acquire a company in the auction process.

Q - Savi Syth {BIO 17476219 <GO>}

That's all. Very helpful. Thank you.

Operator

This is the final call for a question. (Operator Instructions). And this concludes today's question-and-answer session. I would like to invite Mr. Kakinoff to proceed with his closing remarks. Please go ahead, sir.

A - Paulo Kakinoff {BIO 5160310 <GO>}

Okay, ladies and gentleman, I hope you find our presentation and Q&A session helpful. Our Investor Relations team is available to speak with you as needed. Thank you very much and have a nice day.

Operator

This concludes the GOL Airlines conference call for today. Thank you very much for your participation and have a nice day.