

## Q2 2006 Earnings Call

### Company Participants

- Anna Cecilia Bettencourt, Head of Capital Markets & IR
- Antonio Luiz Pizarro Manso, CFO
- Marcelo Rodrigues, Controller
- Mauricio Novis Botelho, CEO

### Other Participants

- Daniela Bretthauer, Analyst
- Heidi Wood, Analyst
- Jander Medeiros, Analyst
- Joe Nadol, Analyst
- Kirby Harrison, Media
- Raymond Neidl, Analyst
- Rodrigo Goes, Analyst
- Ron Epstein, Analyst
- Stephen Trent, Analyst

### Presentation

#### Operator

Good morning, ladies and gentlemen. And welcome to the audio conference call that will review Embraer's Second Quarter 2006 results. Thank you for standing by. (Operator Instructions) As a reminder, this conference is being recorded and webcasted at [www.embraer.com](http://www.embraer.com).

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

The words believes, may, will, estimates, continues, anticipates, intends, expects. And similar words, are intended to identify forward-looking statements. Embraer undertakes no obligations to update publicly or revise any forward-looking statements because of new information, future events or other factors. In light of these risks and uncertainties, the forward-looking events and circumstances discussed on this conference call 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. Maurício Botelho, Chief Executive Officer, Mr. Antonio Luiz Pizarro Manso, Chief Financial Officer, Mrs. Anna Cecilia Bettencourt, Head of Investor Relations. And Marcelo Rodrigues, Controller.

I would now like to turn the conference over to Mrs. Anna Cecilia Bettencourt. Please go ahead.

## **Anna Cecilia Bettencourt**

Thank you for joining our conference call, to discuss our Second Quarter 2006 results, in U.S. GAAP. That we released last Friday, simultaneously with the financial statements in Brazilian GAAP. We are webcasting this conference call with a slide presentation on our website at [www.embraer.com](http://www.embraer.com). I invite you all to follow with -" to follow it.

Now Mauricio Botelho will present the highlights of the quarter. Thank you, Mauricio.

## **Mauricio Novis Botelho** {BIO 13386065 <GO>}

Good morning, ladies and gentlemen. It's a pleasure being, again with you, to discuss our results for the Second Quarter. And the first-half of the year.

I think that this -" in this quarter, we followed a general trend that we were seeing in the First Quarter. We were working very strongly, in the way, to put our new aircraft family in good service conditions in the different customers, while we are spreading the customer base.

On June 5, Embraer concluded its restructuring process. And started to be listed on the new market segment, Novo Mercado segment at the BOVESPA. On May 2, Embraer introduced, during the EBACE at Geneva, the Lineage 1000, one -" an ultra-large business jet, based on the Embraer 190 commercial jet platform. We have had very, very interesting returns from the market in that respect.

JetBird acquired 50 Phenom 100. And placed an order for additional options for 50 aircraft, which makes it a very significant -" will make it a very significant operator for this aircraft.

Embraer 195 airliner, the largest of the Embraer 170/190 family, the last one of that family, received in June, type certification from the National Civil Aviation Agency, ANAC, the Brazilian certification authority. Immediately after, beginning of July, just two days after, we received the European certification as well.

Copa Airlines exercised its options for three additional Embraer 190. And Embraer, in this period, reached an agreement with Kawasaki Heavy Industries to -- in respect on the

transference of responsibilities of the Embraer 190. And 195 wing assembly to Embraer. In that respect, we -- it was a significant move and create to, allow us to control delivery times. And quality on what was being -- that was being supplied.

The results which we -- will be commented, just in a few minutes, by Anna Cecilia, led Embraer to reinforce its solid financial and economic position. During the quarter, Embraer achieved a net profit of US\$139m, with a net margin over 13%, as well as a net cash of \$527m.

At the same time, the total backlog was stable at the \$10 billion level. And, for our satisfaction, we saw the executive jet market responding very well to our products. During Farnborough Airshow, we disclosed a firm order backlog, of over 235 firm orders for the Phenom 100 and Phenom 300. And with a total value for this executive jet backlog for all models, in the region of \$1.25b. The Legacy 600 is also doing very well, delivering two aircraft, in some month's three aircraft, next open position just before June/July of next year.

So I think that these results show that, we are on the right path. And I'll pass the word to Anna Cecilia, to present the figures on the different aspects of our quarter. Thank you. I'll be back later.

## **Anna Cecilia Bettencourt**

Thank you, Mauricio. During the Second Quarter 2006, we delivered 36 aircraft, nine more than in the First Quarter 2006. And six more than the number delivered in the same period last year. Out of the total 145 aircraft expected to be delivered in 2006, we delivered 63 in the first-half of the year.

Net sales this quarter reached \$1b, a 25.7% increase over the same period last year. And 26.4% higher than the previous quarter. This increase is mainly because of a higher delivered, as well as a better product mix with a higher value.

Gross margin, the Second Quarter 2006, was 26 -- 28.2% compared to 31.4% in the Second Quarter 2005. While gross margin remains stable at around 28% in the best reported. This decline is mostly due to E-Jet's learning curve, associated with the beginning of the production of the Embraer 170, Embraer 175 and Embraer 190. In addition, gross margin was negatively impacted by 11.7% appreciation of the Reais against the U.S. dollar period-over-period.

Commercial Airline net sales increased 38% over the same period last year. And reached a 70 -- \$739.9m, representing 22 -- 72.5% of our total net revenue this quarter. Also, revenue for the Executive Aviation market increased by (50%) when compared to the Second Quarter 2005, as a result of higher number of Legacy 600 delivered during the quarter.

Customer Service and other segments also presented an increase in revenue, reaching \$131.1 million compared to \$98.6 million in the Second Quarter 2005. And representing

FINAL

12.8% of total revenue. On the other hand, Defense and Government sales represented 5.9% of our total net revenue, reaching \$60.2m, a decrease over the \$116m, recorded in the Second Quarter 2005.

Despite the appreciation of the Reais against the U.S. dollar, income from operations reached \$134.9m, representing a 36.4% increase, compared to income from operations, for the same period last year. This increase is mainly due to the recognition of \$57 million in research and development revenue. Related to an agreement reached between Embraer and Kawasaki Heavy Industries Ltd, in which we will take operate -â€" we will assume the assembly of the Embraer 190. And Embraer 195 wing -- wings, in order to meet the growing demand for this type of aircraft.

Higher operating results led to an increase in net income and net margin, which totaled a record \$139.1 million and 13.6% in the Second Quarter 2006, compared to \$83 million and 10.2% in the Second Quarter 2005.

During this quarter, trade accounts receivable remain relatively stable at \$472m. Of this total amount, approximately \$140 million is related to aircraft delivered, for which sales financing arrangements are under structuring process.

During this quarter, also inventories remained stable at \$1.6b, compared to \$1.647 billion in the First Quarter 2006. As a result of higher bottom-line results, net cash increased by \$224.2 million to \$526.9m, a strong indicator of the Company's high level of liquidity.

Short-term and long-term loans, excluding non recourse debt, increased by \$137 million to \$1.5b, of this amount, 59% is long-term and 41% is short term. The average dollar cost of our debt was 7.1%. And the Reais cost portion was 9.5% this quarter. The long-term credit lines are due to mature between 2007 and 2011. And have an average lifetime of about two years and one month.

At the end of the quarter, we reported a firm backlog of 209 -â€" firm back -â€" firm Commercial Airline backlog of 298 jets, including six aircraft from the ERJ145 family. And 292 aircraft from the Embraer 19 -â€" 170/190 family. Firm orders for the Phenom 100 and Phenom 300 reached more than 235 units at the end of the quarter. Also at the end of the quarter, our firm order backlog reached \$10.2b, of which \$1.25 billion was related to Executive Aviation segment.

We maintain our forecast, for deliveries of 145 Commercial, Executive and Defense aircraft, which includes only executive transport aircraft in 2006 and 150 aircraft in 2007.

So now we will open this conference call for question and answers. And thank you.

## Questions And Answers

### Operator

Ladies and gentlemen. we will now begin the question and answer session. (Operator Instructions) Our first question comes from Joe Nadol of JP Morgan. Please go ahead.

**Q - Joe Nadol** {BIO 3056499 <GO>}

Yes. Good morning, hello. I have two questions the first is on selling expenses in the quarter. The press release explained why they are -â€" where they are. And a lot of it has to do with the Corporate Aviation build-out. But I'm wondering if you can classify, or help us understand, how much of these expenses is ongoing versus one-time in nature?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Hello Joe. It is, in fact. And in this aspect, we have a lot of efforts in terms of putting together, the selling structure for the Executive Jet business, which has expanded very much. And, on the counter part, you do not have the respective revenues to be generated for that part. This, by itself, represents a distortion, on an ongoing process. If we were already delivering the aircraft, we would have that coming to a balanced situation. Today we are expanding but no revenue.

The other point is that, we are still working hard in improving the operation parameters of our new aircraft in service, the 170 and 190. We are having very good progress. But still we are working hard in that direction, which represents also significant expenditures.

You see that a lot of this effort, which is significant, has been done in this first-half of the year. At the same time, while we increased our deliveries, the largest portion of our deliveries will happen in this Second Quarter. And then the balance, the overall balance, will decrease. However, at this quarter, it still shows a higher, what I would say, a bigger proportion than what would be expected in the future.

**Q - Joe Nadol** {BIO 3056499 <GO>}

So, on an absolute basis though, do you expect -â€" yes, I understand that as a percentage of revenues they will decline, because your revenues are growing. But do you expect them to remain the same or grow on an absolute basis?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

It is going down, yes.

**Q - Joe Nadol** {BIO 3056499 <GO>}

It will go down on an absolute basis.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

It will go down, yes.

**Q - Joe Nadol** {BIO 3056499 <GO>}

FINAL

Okay. The second question is on Defense. And Defense sales are coming in, obviously down from last year. And I think a little bit shy of your expectations. Could you give some color on what your expectations are for the back-half of the year? And any important orders that are out there that might help some?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

In the Defense market I don't expect significant orders. We are fighting in two international bids, which are of relevance. Probably there will be one decision coming out by the end of the year, which is a Turkish bid on the new Trainer. But the Singaporean one, which will be most likely in the next year.

But what is -â€" we are, in fact, today, very much dependent on the Brazilian Air Force action, in that respect. And the revenues are going down, because of the budgetary constraints in this with our customer. I don't expect significant change in the Second Quarter, in this specific business.

**Q - Joe Nadol** {BIO 3056499 <GO>}

Okay. And in terms of the market outlook for international sales of Airborne Early Warning Aircraft, is there -â€" are there any prospects, or is that market slowing down quite a bit?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

There are prospects, however, we do not expect anything to happen in the short/medium time.

**Q - Joe Nadol** {BIO 3056499 <GO>}

Okay. All right, thank you.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Thank you, Joe.

**Operator**

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

**Q - Ron Epstein** {BIO 1868102 <GO>}

Yes hello. Good morning. Mauricio, to start, a quick question for you, you mentioned the costs, associated with supporting the roll-out of the 190, (the entire) in the first-half of the year. Can you give us just a better understanding of how much lower that will be in the second-half of the year? What's changed in the second-half of the year, versus the first-half of the year in terms of supporting a roll-out?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Bloomberg Transcript

Of course, Ron. And pleased to talk to you. The point is that what has happened the first-half of the year, we were having problems with the aircraft, with the systems, with the training of the -- our customers' pilots and mechanics. So we address it; a huge effort. And we had to have those issues corrected. They are, most of them, are corrected.

So, what happens is that we address it, with this effort, a significant expenditure, which (totals) the resolution of problems, which will not be maintained in the Second Quarter and quarters ahead of us. So I really expect this expenditure to decrease in volume, because the problems will have been solved. And they will not have to be repeated again.

You will always -- you will have expenditures, in terms of the increased service, of an aircraft in any airline. But what we were dealing with was a problem of an entry service situation for the product. And these problems that were -- that shown up -- have shown up in this start-up, they are going to be solved. Most of them are already solved and they will disappear in the next -- in the future. And we will have just the normal entry service process that we'll be taking care of.

**Q - Ron Epstein** {BIO 1868102 <GO>}

Okay great. And just another follow-on question to that point. And this is for Anna and Antonio. You'd spoken, earlier this year, about having a gross margin target of about 30% for the year. Do you still maintain that target?

**A - Anna Cecilia Bettencourt**

Ron, well if you compare. And if you take into consideration, the devaluation of 11% that, we experience period-over-period, our gross margin would be around that. So if you consider that between 10% and 15% of our total cost of goods sold are denominated in Reais. And you apply this 11%, this represents 150 -- more or less 150 basis points. Impact on our margin is only due to the devaluation.

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

And it will be possible through the end of the year to achieve almost the 30%.

**Q - Ron Epstein** {BIO 1868102 <GO>}

So you still think by the end of the year you can get that 30%.

**A - Anna Cecilia Bettencourt**

But, again, everything depends on the currency fluctuations, because of this Reais portion of our cost of goods sold.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

But the trend we have seen so far is that, the curves are getting together, they are matching. So we do not expect the same devaluation on the dollar that we have seen and lived with in the last quarters, they are getting together. And we see this very clearly in the average cost of our inventories. It's getting closer to the costs. I mean, if you take the

average exchange rate, for the inventories, if you compare it with the average exchange rate, for the revenues, they're getting together and the trend is to match both.

## A - Anna Cecilia Bettencourt

In Brazilian GAAP, we know that you do not follow the Brazilian GAAP. But in Brazilian GAAP we saw already some improvement, in terms of our gross margins, because of this trend.

## Q - Ron Epstein {BIO 1868102 <GO>}

Good, very good. Just two last questions. And then I'll move on I'll let someone else ask. Mauricio, could you just give us a quick update on the status of the current sales campaigns with the 170 and 190?

## A - Mauricio Novis Botelho {BIO 13386065 <GO>}

Well I think that there are -â€" that there are, today, very good campaigns in process of having a decision. And I think that -- I expect, at least, to have positive, very positive answers in the near future. And I cannot comment (inaudible) in process. But I do expect significant good news in the near future.

The point you saw the industry earlier this -â€" I mean it was July, August -â€" July, end of July, we already achieved a significant order from Republic, comprising 30 Embraer 175's. This was very important. And we expect more for this year.

## Q - Ron Epstein {BIO 1868102 <GO>}

That's great. And then one last final question â€" if you could just give us some color on, what happened with Kawasaki Heavy? In terms of why Embraer had to bring the production of the 190 and 195 wings in-house?

## A - Mauricio Novis Botelho {BIO 13386065 <GO>}

We have a problem of quality. And we have the problem of compliance to time schedule. And then, as it was not solved, we took it from them and we have the control of it now.

## Q - Ron Epstein {BIO 1868102 <GO>}

Okay that's great. Thank you, Mauricio.

## A - Mauricio Novis Botelho {BIO 13386065 <GO>}

Thank you.

## Operator

Our next question comes from Raymond Neidl of Calyon Securities. Please go ahead.

## Q - Raymond Neidl {BIO 14015874 <GO>}



Good morning, everyone.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Hello, how are you doing?

**Q - Raymond Neidl** {BIO 14015874 <GO>}

Just a couple of further clarifications on the 170/190. As far as Varig goes, it appears that, they may end up becoming a big customer of yours. I just wanted your assessment on your chances of them, expanding the way they want in Brazil, or even surviving?

And number two, what your chances are of maybe getting that order versus Airbus?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Well, Varig is living today, what probably could be a new situation, a deeply new situation. It was the -â€" a portion of Varig, the so-called (good) Varig, was sold. A group has acquired it and this group, about 80% is formed by Varig-LOG. And those who acquired Varig-LOG. And 20% is a portion of 10% from Air Canada.

So, I think that, today, Varig is receiving entrepreneurial skills that probably they had forgotten for a long time. They have -â€" they are focused on recovery with a good, excellent track record from one of the -â€" at least one of the shareholders. And they have a big fight with them, at this moment, to make things happen.

At this -- and this, what I'm going to say is just commenting because it was public, it was reported in the press. And Varig is really looking for new aircraft and they are considering very strongly Embraer 190, as they say. So, of course, this is not an easy situation. But this is something to be looking at very carefully. And we are very close to them, trying to make things happen.

**Q - Raymond Neidl** {BIO 14015874 <GO>}

You would not get involved, if they were to put in a significant order to you for the 190. You would not get involved with financing those aircraft, or you wouldn't have any of that type of risk, would you?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

No, not at all.

**Q - Raymond Neidl** {BIO 14015874 <GO>}

Okay great. The second thing is JetBlue, they were having some problems introducing the 190. I'm just wondering from your viewpoint, are those problems all cleared up now?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

No, not all of them are clear, no. A lot of them are cleared now. What we are seeing is that, as far as the reliability. And the (specialty), has improved very substantially, some of the solutions are not stable at this moment. So -â€” but we have the firm belief that this is going to be definitely solved in a very short period of time. But all the operation parameters have improved, very significantly, from where we started earlier this year.

**Q - Raymond Neidl** {BIO 14015874 <GO>}

Okay, there's no slowdown in your delivery schedule to them?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

No, we are moving as planned.

**Q - Raymond Neidl** {BIO 14015874 <GO>}

Great. Thank you, very much.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Thank you. Welcome.

**Operator**

Our next question is from Heidi Wood with Morgan Stanley. Please go ahead.

**Q - Heidi Wood** {BIO 3095506 <GO>}

Good morning, guys.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Hello Heidi.

**Q - Heidi Wood** {BIO 3095506 <GO>}

Hello, Mauricio. How are you?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Very well. And you?

**Q - Heidi Wood** {BIO 3095506 <GO>}

Good, good. Mauricio, I want to ask you a little bit -- to give us some color on your pricing strategy for the E-Jet. We are looking at yet another banner order here for A320's and 737's on top of a very strong '05.

When you look at the pricing of the 190, your upper-end planes, in the 24 million arena, when the Boeing and Airbus planes are at the bottom end, being priced at about 30m,

do you feel that you need to widen that pricing gap i.e. lower your price to get greater market reception?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Heidi, what I see is that, unfortunately, what we have been facing is not that sort of price from our competitors. The fight is much tougher than this one that you are mentioning. And the point is that, we are not decreasing price for -â€" just to maintain absolute monopoly's position, not at all. And this, of course, is not happening, as you are seeing in the -â€" when you analyze what's happened with the airlines.

The point is that the pricing, from our competitors, is something -â€" this -- very much aggressive. And what we are doing is that we are fighting to make things happen.

**Q - Heidi Wood** {BIO 3095506 <GO>}

Yes. Well no, that's -â€" I know we can see the headwind. Can you give us a view? Maybe take a stake in the sand, without naming names, how many new operators, other E-Jets, you foresee, could be announced next year, within the next year?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

It is difficult to make this -â€"; to spell it out. It is difficult, because we have places in which we are, for years, expecting things to happen. As the next Board Meeting, the next Board Meeting. And the Board Meeting does not address their attention to the issue. So I think it will -- maybe it will not be a firm guidance that we can do in (commenting it).

What I say. And I reaffirm that, is that I am very confident that we may have good news, very good news this year. How many will come next year, I prefer not to comment, because it may give the -â€" give wrong evaluations on the future. I cannot say.

**Q - Heidi Wood** {BIO 3095506 <GO>}

Okay, may I take one last stab out here? There -â€" it looks like Boeing and Airbus are pushing out the timing when they may do a new narrow body replacement. And I've heard you talk, at different times, about the merits of potentially being a supplier. And on some occasions potentially addressing that niche as an OE. How does a delay, in entrance of the two big players in this market, in any way change your thinking towards attacking that market niche?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Heidi, I always see this situation, with the perspective on -- based on what has happened in the past. Today, of course, we have studies towards a new narrow body. Of course, we look at every niche of the market, to understand it. And to see what can -- what the ideas may be. However, the best we could do, today, is a similar aircraft to what already exists and this means a disaster.

FINAL

Bloomberg Transcript

FINAL

So, I think that all this issue of a new narrow body, it is in reaction or in connection, with the ability of having a new revolutionary engine. If this does not happen, there will be no reason to have a new narrow body. Because the smaller the aircraft is -â€ the smaller the aircraft is this issue of new fuselage materials. This has very small implication on costs, of course it does. But it's a very small implication. What here really would be a strong point, would the efficiency on the operation of the engine.

But in a bigger aircraft, now then, you start to talk about substituting heavy structure by lighter structures, in a sense that you would make a difference. But today, it doesn't flow to make any big thing if you now have 126 seat aircraft -â€; 136 seat aircraft, you substitute a cheap raw material, such as aluminum by an expensive material, such as composite. And a different sort of composite. The impact would be very, very small.

We keep looking at that. And we keep saying that we are not interested in being a supplier, if something in the future may come. Because I think that we have capabilities that are differentiated, when you compare with other suppliers. I don't think that the best approach that, we can have in the aeronautical industry, is low-cost manufacturing.

There are other planes which you can achieve low costs. But there are no other planes that, you can find the consistency of engineering, with the ability to conceive to develop, to certificate and manufacture, to work in a simultaneous basis with conceiving and developing to achieve the best development costs.

This is what makes us different. And as that I don't see us as a supplier. What I see is that, if anyone would see value without contribution, it should be value as a business partner, not as a supplier.

But all of this has only to do with my thoughts. And they are very far from anything that may be assumed as a reality. So, at this point I think that, the Embraer 170/190 jet family is well placed in the market. They represent a good mix of products for our customers. And we are not competing in the narrow body. And I don't see them being competitive, very strongly competitive, unless other circumstances are put together in the same deal with other aircraft, because it is a matter of reality.

Our aircraft weighs -â€; the 190 weighs 15 tones less than the Airbus 1818, 13 tones less than an Airbus A380, if you go to 737/700 it is about the same proportion. So, unless other circumstances are put together, in a same deal that, could overcome this fact of life issues, as weight, performance and cost of the aircraft, then I think that we'll have a good position.

**Q - Heidi Wood** {BIO 3095506 <GO>}

So you're saying -â€; that's an excellent answer Mauricio, thank you. But you're saying that net, net you're still getting out maneuvered somewhat, because Boeing and Airbus are wrapping these into package deals?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Bloomberg Transcript

Sorry, Heidi, I couldn't understand your statement. Could you please repeat it?

**Q - Heidi Wood** {BIO 3095506 <GO>}

Yes, absolutely. When you say other circumstances, I just want to make sure I understand you clearly. Are you saying that Boeing and Airbus are, in some ways, out maneuvering you? Because they're wrapping their single-isle deals into package deals for upper-end airplanes as well.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Yes, what I understand is that, if a certain operator has a fleet of Airbus' or Boeings and they are really something like 126 seat aircraft, maybe, it may be the case that instead of acquiring Embraer 195, or even an Embraer 190 they have reasons to keep with the same aircraft type. And this is "I cannot do anything about that. And this is the point.

However, I think there is a market, a growing market that is looking for specific operational efficiencies. And in that case we will be the winners. Let's see at JetBlue, look at Air Canada, you can look at Fin air. And you have several examples of airlines who -- where we have disputed with Boeing or with Airbus and we won. There are others that we lost.

**Q - Heidi Wood** {BIO 3095506 <GO>}

Right. Thank you, very much Mauricio, I appreciate that.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Good to talk to you.

**Operator**

Your next question is from Stephen Trent with Citigroup. Please go ahead.

**Q - Stephen Trent** {BIO 5581382 <GO>}

Good morning, Mauricio, thank you, how are you?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Good morning, how are you? How are Portuguese doing? Better?

**Q - Stephen Trent** {BIO 5581382 <GO>}

One or two quick questions for you sir. And thank you for the greeting.

As a follow-up to Ron Epstein's question earlier, I'm just trying to get hands around this \$57 million gain in R&D. So you're basically, if I understand correctly, you've taken over these local operations from Kawasaki. And you're recognizing this gain upfront, as opposed to matching it with your per-unit sales going forward? Is that a correct assessment?

FINAL

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

That is correct. Because U.S. GAAP â€"; we see that U.S. GAAP asked for the recognition. If you go to the Brazilian GAAP it would be amortized along the time and deliveries.

**Q - Stephen Trent** {BIO 5581382 <GO>}

Okay, very clear. And just one or two other quick ones for you, Mauricio. When I saw you last month, in London, there wasn't much going on in terms of the South American market, with respect to military contracts and I was looking for an update. Since that time, it looks like Venezuela is buying some jets from the Russians. I was wondering if you're seeing, with respect to this, if there's any change in dynamics in the South American military market.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Well, officially I don't see anything happening. My perception is that, as far as the supply of jets to the Venezuelan Air Force, maybe other Air Forces will look for similar capabilities.

**Q - Stephen Trent** {BIO 5581382 <GO>}

Great. And just one last question Mauricio. If I'm not mistaken, Boeing recently entered into an agreement with respect to its supply of titanium. I was wondering what is Embraer's strategy, with respect to this raw material going forward?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Very recently, we agreed with this Russian Company, DS & D something, a long term contract for supply of titanium, to fulfill our requirements â€"; in how many years?

**A - Anna Cecilia Bettencourt**

I think it's more than five years.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

In more than five years. And, much more to 10, than to five. So we are comfortable in that respect.

**A - Anna Cecilia Bettencourt**

We announced this deal during the Farnborough Air Show, Steve.

**Q - Stephen Trent** {BIO 5581382 <GO>}

Great. Okay, I'm sorry I must have missed that. (inaudible).

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

Steve, just to complete the information, the \$57 million will be retrieved on the (equity) payment of roughly \$8 million (mark).

Bloomberg Transcript

**Q - Stephen Trent** {BIO 5581382 <GO>}

Perfect, thank you very much.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Could to talk to you Steve.

**Q - Stephen Trent** {BIO 5581382 <GO>}

Same here.

**Operator**

Your next question comes from Jander Mederios of Banco Pactual. Please go ahead.

**Q - Jander Mederios**

Hi everyone, just a quick question regarding the agreement that you've signed with Kawasaki. Should I expect an increase in CapEx, since you are now responsible for assembling the wings? That's my question, thank you.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

No, the factory is there, the problem is mostly on management. And the ability to be flexible and present quality. All the CapEx is there and if there is something else necessary it will be an irrelevant amount. Just a minute, Marcelo has a compliment.

**A - Marcelo Rodrigues** {BIO 22132956 <GO>}

Yes, on the CapEx it means that we have to do some engineering work, which is excluded from this \$57m, about \$8 million on investments, which is read as an asset to be consumed over the next few months.

**Q - Jander Mederios**

Okay, thank you.

**A - Marcelo Rodrigues** {BIO 22132956 <GO>}

The \$57 million is the \$57m.

**Operator**

Your next question comes from Rodrigo Goes with UBS.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Good afternoon.

FINAL

Bloomberg Transcript

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Hello Rodrigues.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Just a couple of quick questions on -â€" most of them -â€" most of my questions have been answered already. Just with regards to the contribution from risk sharing partners, I was wondering if you could us guidance with regards to future recognitions of contributions. And how that will affect your R&D expenses going forward?

And the other question was, if you could give us an idea of how many of your targeted deliveries, for this year and next have already been slotted?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

That's a good one.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Hello?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Hello.

**A - Anna Cecilia Bettencourt**

Yes, we are here.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Okay.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

For this year it is fully done. Next year it is, unless very few manage, because the Legacy's we have open position until just from July on. So, I can say that from 150, maybe, we're talking about 10 aircraft, Executive Jet, on the airline market we're done.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

So for this year you're -- the 145 have been fully slotted?

**A - Anna Cecilia Bettencourt**

Yes, we are sold out for '05.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

'06.

FINAL

Bloomberg Transcript



**A - Anna Cecilia Bettencourt**

'06, I'm sorry. And for '07 we have very few slots available.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Okay.

**A - Anna Cecilia Bettencourt**

For the Legacy. And for the Commercial Airline we are sold out.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Okay. So, are you trying to say that, this year you're most likely to beat your delivery target of 145, even though you're sticking to it?

**A - Anna Cecilia Bettencourt**

Yes, that 145 is the delivery guidance. And we're sticking on that 145 number of deliveries.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

We are working in the expansion of our production capabilities and deliveries. And however. And we are doing that. And our forecast already considered expansion in our production capabilities. But we are doing it further. However, the speed in which this can be accomplished, due to the complexity of the supply chain, is not that much. We are foreseeing reaching a significant "not significant. But a reasonable increase further by the First Quarter of 2008. (inaudible).

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Just on that same issue is it fair to say that, the 145 target for this year is within the limits of your current supply chain capabilities?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Today, today it could increase the Legacy's "today we could increase the Legacy's and the AJ 145's. And this is the only thing that we can do today. The expansion of the production line for Embraer 749 -- 190 it is on course. And what I said, we are expanding our 150 deliveries considers this expansion. And at the same time, we are further expanding to -- looking forward to 2008.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Got it. Okay, perfect.

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

Rodrigo, about the contribution for 2006, we expect to have an additional, the recognition of additional of \$33 million in the second semester of the year, regarding the accomplishment of some contractual milestones.

FINAL

Bloomberg Transcript

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

And in '07?

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

In '06, second semester.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

And anything in '07?

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

Around \$45m.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Okay. And that \$45m, is it more or less spread out evenly throughout the year?

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

Yes, I think it's much more concentrated in the second semester.

**Q - Rodrigo Goes** {BIO 6232382 <GO>}

Okay, very clear. Thank you, very much.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Thank you.

**Operator**

The next question comes from Daniela Bretthauer with Santander.

**Q - Daniela Bretthauer** {BIO 13380169 <GO>}

Hi. Good afternoon everyone. Most of my questions have been answered. But two quick questions on your working caps, though you seem to be doing pretty well, in terms of both receivables and inventories so far, in the first-half. Should we expect a similar trend for the second-half in terms of both inventories and receivables? That's my first question.

**A - Anna Cecilia Bettencourt**

Yes Daniela. We expect to see "€"; we are seeing a very stable line, a situation with the accounts receivables and the inventories, around 1.6. A very comfortable situation and we expect to the same (inaudible) in the second-half of the year.

**A - Marcelo Rodrigues** {BIO 22132956 <GO>}

Almost delivered for this year just had to do financing to prepare it. We don't go to assuming some (inaudible) in our accounts receivables that's the (strategy) to date, we go to (inaudible) at the end of the year our accounts receivable.

**Q - Daniela Bretthauer** {BIO 13380169 <GO>}

Okay. Great. And in terms of a gross margin guidance, you're around 28% now. And you haven't exactly quantified the e-learning curve impact and the effects. But in terms of gross margin guidance, should we expect around 28% also for the second-half of the year? Or what sort of guidance can you give us in terms of gross margin?

**A - Anna Cecilia Bettencourt**

Daniela, it really depends on the exchange rate, okay. If you look at our cost of good sold composition about 10% 15% of this is denominated in the local currency, in Reais. So 11.7% depreciation of the currency for our -- from last quarter, means that from the Second Quarter '06 comparing to Second Quarter '05 represented an impact of 120 basis, 150 basis points in our gross margin. So, if you add this back we would be around 30%. So the guidance is to be around 30%, it really depends on the currency situation that we might be seeing in the second-half of the year.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

But, however, as we counted before, we see that the average exchange rate for inventories is -â€" the trend is to match with â€"; they are very close today â€"; trend to match with the average exchange rate for the revenues. So the impact tends to be less significant. So we are looking at a 30% gross margin at year-end.

**Q - Daniela Bretthauer** {BIO 13380169 <GO>}

30% at the year-end. Let's say assuming the Reais stays around this level, average effect of around (BRL2.17) for the second-half, at least that's the Santander guidance. But let's say BRL2.17 for average effects for the second-half of the year, you think it's possible that you end the year with a 30% gross margin, that's what you're saying basically?

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

In the last quarters we believe must have something the difference of this, it would be possible for achieving 30%.

**Q - Daniela Bretthauer** {BIO 13380169 <GO>}

So, is it also true that, towards the end of the year, the impact of the e-learning curve will be over or do we expect more in 2007?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

We're expecting it to go down very, very steeply in the second-half of this year. Because the huge effort that was put on in the first-half, it will not be repeated. But the question that we faced, at that time, has been solved, it is not all of it solved but they will be solved soon. But by far, the largest amount of problems, are over now. And so we will not be

repeated the next quarter. But we did have is just normal entry services in the different airlines. And normal entry services (course), which has nothing to do with the magnitude of the effort that was put together in the first-half of this year.

**Q - Daniela Bretthauer** {BIO 13380169 <GO>}

Okay, thank you.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Thank you.

## Operator

(Operator Instructions) Your next question comes from Kirby Harrison with Aviation International News. Please go ahead.

**Q - Kirby Harrison**

Good morning.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Good morning, how're you doing?

**Q - Kirby Harrison**

Excellent, excellent. You mentioned 235 firm orders for the Phenom 100 and 300, what form were those? Are those non-refundable deposits or MOU's?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

No, they are contracts with cash against down payment. There are more than 235. But, I mean, it's not a letter of intent, it's not only wishes, they are firm contracts with cash against deposits non-refundable down payments.

**Q - Kirby Harrison**

Okay. And do you have a launch customer yet for the Lineage?

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Well, we have one contract signed in a Middle East operator. We are now said it -- there was a press release about it; it was published in the press, here in Brazil, about one week, two weeks ago. It was one aircraft, yes.

**Q - Kirby Harrison**

I see. Thank you, very much sir.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

You're welcome.

## Operator

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

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

Thank you. Well, I have to thank you again for your attention. And we keep working hard to achieve our prospects for the year. We are confident that we are in the right place, on the right track. And I believe that things are getting better and better. And I have confidence in the future.

I thank you again and pass the word to my colleagues here.

**A - Antonio Luiz Pizarro Manso** {BIO 1845027 <GO>}

Thank you, very much from my side.

**A - Anna Cecilia Bettencourt**

Thank you. And we will be talking soon. We will have, in November, our analysts and investors meeting in Brazil, which I believe most of you received already the save the date notice.

**A - Marcelo Rodrigues** {BIO 22132956 <GO>}

Thank you, very much. We welcome any questions that, if you have any, we can answer that through the Investor Relations department.

**A - Anna Cecilia Bettencourt**

And also by September 5, we will be, in September, with the mock-up of the Phenom there, the New York Stock Exchange. So people when we also have the (inaudible) day there, where (inaudible), Mauricio and other executives will be talking about the Executive Jet market, addressing this market. And presenting the product, which is the most important thing.

**A - Mauricio Novis Botelho** {BIO 13386065 <GO>}

And, also with an application list, for those who would like to fulfill an order.

Thank you, very much.

**A - Anna Cecilia Bettencourt**

Thank you. And we will see you there. Bye, bye.

## Operator

That does conclude Embraer's audio conference for today. Thank you, very much for your participation, have a good day. And thank you for using Chorus Call, Brazil.

FINAL

*This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.*