

## Q4 2016 Earnings Call

### Company Participants

- Eduardo S. Couto, Director of Investor Relations, M&A and New Businesses
- José Antônio de Almeida Filippa, Executive Vice President-Finance & Investor Relations (CFO)
- Paulo Cesar de Souza e Silva, President & Chief Executive Officer

### Other Participants

- Alexandre P. Falcao, Analyst
- Bruno Amorim, Analyst
- Cai von Rumohr, Analyst
- Darryl Genovesi, Analyst
- Derek Spronck, Analyst
- Joshua Milberg, Analyst
- Peter John Skibitski, Analyst
- Turan Quettawala, Analyst

## MANAGEMENT DISCUSSION SECTION

### Eduardo S. Couto {BIO 18009973 <GO>}

Hello. Good afternoon, ladies and gentlemen, welcome to the Embraer 2017 Brazil. We are glad, we are all here today to attending this event. We will start with our 2016 financial results and the 2017 outlook. The first part of the event will be broadcast.

Today with us we have Mr. Paulo Cesar de Souza e Silva, our President and CEO; Mr. José Filippa, Chief Financial Officer and myself, Eduardo Couto, I'm the Head of Investor Relations.

Before we start just as a reminder, this conference call includes forward-looking statements or statements about events or circumstances which have not occurred. Embraer has based its 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 other markets where the company is present.

The words believe, may, will, estimates, continues, anticipates, intends, expects, and similar words are intended to identify forward-looking statements. Embraer undertakes no

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.

With that, I would like to turn the conference over to Mr. José Filippa. If you can start.

## **José Antônio de Almeida Filippa**

Okay. Thank you, Eduardo, and welcome again to attending our conference. As usual, we're going to go to the presentation of the 2016 results and also in the 2017 estimates, and then we'll be entering the Q&A session.

So starting the presentation starting in page 3 with the corporate financial highlights for 2016. Considering only the recurring results, the company had a positive year in meeting all the guidance. For the year 2016, the total revenues amounted to \$6.2 billion, the adjusted EBIT of \$499 million with 8% EBIT margin. Total investments were \$630 million and net cash flow was a consumption of \$359 million.

In finalizing the financial results, we closed 2016 with the backlog of \$19.6 billion, adjusted net income of \$291 million, and then earnings per ADS of \$1.58. Our net debt position as of December 31, 2016 was \$575 million.

Over to next page, page 4, regarding Commercial Aviation highlights, we delivered a total of 108 aircrafts in 2016 including the E-Jet number 1,300th, which was an E195 to our Chinese customer, Tianjin Airlines.

With that, we have accumulated firm orders of more than 1,700 aircrafts since the entry into service of the E-Jet family. In terms of the E2 program, first commercial activities reached 275 firm orders of a total of 690 commitments.

And in relation to the development, the E190-E2 still on test flight campaign with 40% completed with the entry into service scheduled for the first half of 2018. And as of last year, we probably had the roll out of the first E195-E2 scheduled to entry into service in 2019. Finalizing the highlights of Commercial Aviation, regarding our service activities, our pool parts program has reached over 50% of all the ERJ customers and 65% of E-Jet customers.

Next page, page 5, moving to Executive Jets highlight for 2016. We delivered a total of 117 executive jets broken by 73 light jets and 44 large jets. Including the executive jets, number 1,000 and the Phenom number 700. In terms of industrial activities, we delivered the first Legacy 450, with final assembly in our Melbourne, Florida facility.

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In terms of commercial activities, we launched two new Executive Jet versions, the Phenom 100 EV and the Legacy 650E. And the Phenom 300 was again the most delivered executive jet in the industry for the fourth year consecutive.

Regarding customer satisfaction, we were ranked number one by both AIN and Pro Pilot's Survey in 2016. And finalizing the highlights of Executive Jets, we ended 2016 with market share of 18% in terms of deliveries, and 9% in terms of revenues.

Next page, talking about Defense & Security business highlights in 2016, starting with the KC-390 development. Flight campaign test continues, as we planned. Two prototypes are now over 1,000 hours of flight in the test. Also, we started the serial production of the KC-390, for the first KC-390 to the Brazilian Air Force. And the first two Legacy 500 for in-flight inspection to the same customer.

The Brazilian satellite program concluded its final tests and is now ready to be launched, which is expected to be in the first quarter of this year. We also signed new contracts for air traffic control modernization in Brazil and abroad. And finalizing really (07:24) highlights for Defense business we inaugurated in 2016 the Gripen Design and Development Center in Brazil, inaugurated at Gavião Peixoto (07:33).

Now moving to the financial results in page 8, starting with our backlog. We reached \$19.6 billion at the end of 2016, and this amount is broken by 70% for Commercial Aviation, 23% for executive - 22% for the Defense & Security and 7% for Executive Jets.

In next page, in terms of deliveries starting with Commercial Aviation on the left. We delivered 108 aircraft in 2016, around 80% of those deliveries were E175, percentage is similar to the previous year. On Executive Jets, on the right side, we delivered 117 aircrafts, as we said broken by 73 light jets and 44 large jets. For both jets - both business units, we were within the guidance range of 105 to 110 jets for Commercial and 105 to 125 for Executive.

Next page, regarding net revenues. We reported a total of \$6.2 billion in 2016, on the high end of the guidance range and 5% above 2015. If we break the net revenues of 2016 by business units, we will have 57% related to Commercial, 28% for Executive, and 15% for Defense. Also in terms of revenues, we met the guidance range of \$5.8 billion to \$6.2 billion in the year.

Next page, net revenues by segment and by quarter. Fourth quarter was the strongest quarter for all the business units. And, going to each business unit, starting with clockwise way, Commercial Aviation, on the top right, we reported a total of \$3.53 billion in 2016, within the guidance, and in the bottom right, Defense & Security reported \$0.93 billion in 2016, slightly above the guidance range with a very strong fourth quarter. Moving to Executive Jets in the bottom left, the total of \$1.73 billion in 2016, higher - in the high-end of the guidance range. And closing the page, on the top left, as already mentioned, the total of \$6.2 billion in the 2016 for Embraer in the consolidated base.

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Next page, page 12 regarding SG&A expenses. Reflecting our focus on cost control, we had a reduction from 2015 with total SG&A expenses of \$533 million in 2016, being \$164 million for general and administrative expenses, and \$369 million for selling expenses.

Next page, as far as operating result, in order to have a fair comparison, we excluded from the reported EBIT the non-recurring items, which were the (11:20) highlighted on the box on the right, that will show the exclusion with a positive impact of the recovery of American Airlines Chapter 11 in 2013. In 2015, the provision for Republic Airways in - of \$101 million, and in 2016, we excluded three items with the partial recovery of the Republic Airways of \$52 million, the voluntary dismissal provision of \$117 million negative, and also the impact of this FCPA settlement of \$228 million with a total of \$293 million in 2016.

So with that, we reported adjusted EBIT of \$499 million in 2016 with an 8% margin both in the high end of the guidance range of - between \$405 million to \$500 million and margin of 7% to 8%. EBIT margin broken by segment in 2016 were in Commercial Aviation 12.3%, Executive Jets positive 1.3%, and Defense positive 4.1%, so all business was positive in the full year basis.

Next page, adjusted EBITDA. We had the same thing mentioned (12:53) in the previous page. We had a total of \$829 million in 2016 with a 13.3% margin. For both amounts in margin we reached the guidance range.

In next page adjusted net income. We had a total adjusted net income of \$291 million in 2016 with net margin of 4.7%.

Next page, page 16. In terms of earning per ADS and payout ratio, we had \$1.58 per ADS in 2016 with a payout ratio of 25%.

In page 17, in terms of investment, we invested a total of \$630 million in 2016, broken by \$48 million in research, \$381 million in development and \$201 million in CapEx, in line with the outlook for the year.

In next page, page 18, as far as free cash flow, although we had the positive free cash flow in the fourth quarter, we ended the year with a consumption of \$359 million, in line with the guidance. The main reason for the cash consumption were the heavy investments in these two programs reflecting in addition (14:29) intangible assets and higher working capital requirements mostly related to the aircraft inventory.

Next page, page 19 regarding Embraer capital structure through debt and cash. At year-end, we had a total debt of \$2.76 billion (sic) [\$3.76 billion] (14:53) and in terms of cash our position at the end of 2016 was \$319 million (sic) [\$3.19 billion] (15:02), which returns to a net debt of \$575 million. In terms of average years in terms of the debt, our debt was 5.3 years at yearend. As you may know, in early 2017 we issued a new 10 year bond of \$750 million and after that the average terms of our debt will increase to 6.3 years.

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Okay. With that, we conclude the financial results and move into the 2017 outlook. In page 21, deliveries and have revenues outlook for 2017. From the left, in Commercial Aviation, we expect to deliver from 97 to a 102 aircraft and revenues in the range of \$3.25 billion to \$3.4 billion. For Executive Jets, deliveries are expected to be between 105 to 125 aircraft, broken by 70 to 80 light jets, 35 to 45 large jets. Revenues for Executive Jets are expected to be in the range of \$1.6 billion to \$1.75 billion. On Defense, our expected revenues will be for 2017 in the range of 0.8 to \$0.9 billion. And other expenses - other revenues are estimated to be \$50 million. Combining all segments, our consolidated revenues for 2017 are expected to be in the range of \$5.7 billion to \$6.1 billion.

Next page regarding 2017 outlook for results, cash and investments. We expect EBIT to be in the range of \$450 million to \$550 million with 8 to 9% margin. In terms of EBITDA, we forecast the range of \$770 million to \$890 million with 13.5% to 14.5% (17:16) margin. For free cash flow, we are estimating a consumption of \$150 million or better, yet reflecting the investment phase of these two developments. And finalizing 2017 outlook, we are estimating investments \$650 million broken by \$50 million to research \$400 million to development and \$200 million for capital expenditures.

With that, we finalize the presentation, and we're now ready for the Q&A session. Thank you.

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

Okay. We're going to start the question-and-answer section. We will start with the audience first. So if you're here in the audience, and you want to ask a question, just raise your hand, we have a couple of mics in the room. Thank you.

## Q&A

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

Hello. Hi, good afternoon, everyone. Bruno Amorim from Santander. So my question relates to the Commercial Aviation division. If I'm not mistaken, you have 175 firm orders in the backlog to you, and you're planning to deliver 100 aircraft this year. So if you go ahead with your plan, you deliver 100 and you receive no order this year, let's say you - you have 75 left for the next few years. So what does it imply in terms of the risk that in the transition to the E2, the orders eventually not maintaining the current level of deliveries in the upcoming years?

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Okay. So hello, everyone. Good afternoon. So thank you for coming and joining us for the session. So the Commercial Aviation, so you're talking about the E1 only right?

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

Yes.

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**A - Paulo Cesar de Souza e Silva {BIO 17023173 <GO>}**

Yeah. So we will start with a view of (19:20) the E2 next year. So we have to look at our combined numbers. So from next year along, 2018 and on, so there will be E2s as well, all right. So we have to add that to that number. The E2 program is on time. So, we are flying (19:43) with the fourth (19:44) aircraft now. So, we're not anticipating any delays at this stage on the conference, so we're on time. So, we should deliver the first E2 between January and June next year.

So, we are - of course, due to nerve power (20:01) it's a backlog for the future. We are - John Slattery will talk more about that when he presents on the Commercial Aviation. So, we feel that we will have a smooth transition from E1 to E2 like in the next year. So, when we look back years ago, and looking into the future, so we could see a huge gap now. So, of course, we know already that we were able to close these gaps, and I'm sure that going forward, also so we're going to have E2 transition.

We have announced recently the E190 launch order for the Norwegian company Widerøe, and as of yesterday evening or this morning, so we have announced also (21:06) Brazil will be the large customer for the E2-E195. So, all in all, so with that indicates (21:14) more pressure next year like which is the year that we're going to do this transition. But we feel that we'll do a smooth one.

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

Thank you. And all that said, so, is it correct to say that your base case for the next year is you delivering around 100 aircrafts, or is there a real reason that next year it's going to be around 100?

**A - Paulo Cesar de Souza e Silva {BIO 17023173 <GO>}**

So, we don't know yet. So we are at this stage, so we cannot affirm whether or not we will do that, what we know is that we are in less important engagements (21:53) whether or not we're going to close so we don't know, but there is a strong activity going on now.

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

Thank you.

**A - Paulo Cesar de Souza e Silva {BIO 17023173 <GO>}**

Sure.

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

Pete Skibitski, Drexel Hamilton. I was wondering if you could talk about the big B to the Defense revenue guidance in the fourth quarter, maybe talk about what the drivers are and maybe quantify them to the extent that you're able to?

**A - José Antônio de Almeida Filippo**

Yeah, maybe. The fourth quarter, we just have to see the year in a whole because sometimes specific events because of the lowest levels of revenue of the company, especially events may interfere, we have specifically deliveries of four (22:37) in the end of the year and those contracts they were (22:42) differently, were not priced over construction, it was like a delivery that we - sorry as we deliver, so that impacted there but I think we should you see in the yearly basis that is in the quarter, but I think it tends to be like the guidance we set, that's going to be from 0.8, to 0.9 (23:02) be done in next year, it tends to be more distributed.

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

And just one follow-up, I think you gave us the 2016 segment operating margins just directionally, how should we think about 2017 for the three main segments?

**A - José Antônio de Almeida Filippo**

Yeah. It's a low double-digit for Commercial and Defense, and mid single-digit for both the others. That could be it (23:24)

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

Thank you.

**Q - Joshua Milberg**

Hi. Josh Milberg from Morgan Stanley. Just going back to your initial question on the delivery level and also the transitions to E2. I think recently you've talked about some potential sources of incremental demand, one of those being U.S. carriers looking to replace 60 to 70 seaters and another source of potential demand being start-up airlines in China looking, being required actually by regulations to add regional aircraft. And I was just hoping you could update us on your view on those potential sources of demand?

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Okay. Thank you. So I'll make just a few comments on that, and then I'll leave it with John to elaborate more on that because that is in his presentation. So this, you guys are right, I know (24:24) it's very complex. So it's a huge dynamic that's going on now in both sides, right, China and in the U.S., but we continue to see very strong opportunities in these vital markets. So having said that, I will leave you with John to elaborate more later on.

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

Thank you. Turan Quettawala from Scotia Bank. My question was regarding the restructuring that you guys are sort of (25:02) working through right now. Can you give us a sense of how much of the savings are already in 2016 numbers, and how much should we expect sort of incremental savings to come through in 2017?

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

(25:13)

Yeah. Thanks, Turan for question. In terms of the cost savings, the Mission 200 (25:20) that we launched last year, the implementation so far has been super good and on schedule. Let's say, maybe even faster than we previously thought. From the \$200 million, we should capture around \$100 million because we had some offset like the stronger currency, the wage increase that we had last year. But from this \$100 million that we should capture, around one-third was captured last year already in the fourth quarter and two-third will be captured throughout this year.

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

If I may add, Turan. Considering the plan that we have, the next piece of the plan, the larger piece will come from the head count reduction, which we achieved. I'd like to note we recorded a provision for the dismissal. And everything else in terms of the cost for example travel expenses and consultancy, they are already budget. So, all the managers of the company already have this target and they have to comply with that in the targets that I have for 2017 because it's already considering the budget for 2017.

### **A - Paulo Cesar de Souza e Silva {BIO 17023173 <GO>}**

Yeah. If I may add also one more word on that. So, we were not stopping this - in this initiative that we launched last year, the \$200 million initiative. So, we will continue. So the new initiatives will come in order to make our company more efficient right in the cost side. Of course we are working out on the revenue side through this new business unit on services that over time will deliver more revenue. The business jet market also I believe that may pull from now on; I think we have reached the bottom, right already. So, there is upside now for the business jet going forward, like if you look at what's going on in the West and the economies and the - so I believe that the worst is over. So, the combination of a little bit more revenue in the more like efficiencies right in the cost side. So, we believe that we can get additional by market going forward.

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

If I may ask a follow-up quickly. On the Commercial Aviation side with the E2 coming into production and deliveries next year, can you talk a little bit about how much of the losses you're expecting on the E2 next year when the first units are delivered? And maybe or just a number sort of maybe across the whole program, how much of a loss are you expecting on that?

### **A - Paulo Cesar de Souza e Silva {BIO 17023173 <GO>}**

I don't know yet. Of course, any wrap up, of course of a new product, so you have additional cost right at the beginning. But I can't say now, so how much that would be. So, it's already like embedded in our Defense (28:22), because we start already to manufacture the E2 this year, right, so by June, July. So, we will start manufacturing aircrafts for the review of next year. So, our relative cost is embedded in 2017. And you have now our guidance here for 2017 in terms of margins so and so forth. So, it's not bad.

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

And Turan, just to compliment, I think most of the deliveries in 2018 will still be on the E1. And something that has taken into account as well is that even for 2017 we will require of



course the remaining working capital for the starting of the production of the E2. We estimate something around like \$80 million to \$100 million, is all included in the guidance for cash consumption that we send out.

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

If Thank you very much.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Let's get do the webcast question now if we have a chance.

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

Can we take the question from the floor. Operator?

Okay. Here (29:37) from Bank of America Merrill Lynch. Yeah.

Yeah.

Can you please discuss the order pipeline for business jets in the U.S.?

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Can you please be a little bit loud?

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

Sure. Can you please discuss the order pipeline for business jets in the U.S.?

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

The order book.

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

Have you seen any change after the election?

For the markets. Yeah the jet market.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

So markets, market.

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

Yeah Executive Jets.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

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Okay. So well so the business jet market, if you look at the numbers of last year's it's too depressed. And so the market last year delivered 648 units. In the peak of the business jets, the market was in 2008 with 1,300 aircraft. So having said that, we still see a very large inventory of used business jets at around 12% of the number of aircraft in operation. So that's - if that's meaningful that's a loss, right, too many. So, we still need to clear this inventory a little bit, having this inventory down - drop to around 7%, 8% in order to have a more deal flow market, all right. So it's going to take a while. However, we believe that the work is over now. So, from now on, so we can see gradual improvement. But it's not going to be like strong improvement. So it's going to be step-by-step, but very good. I'd say it's more like small improvement.

We believe that we are, with our line of products which are state-of-the-art, so the Phenom 300 being the most delivered aircraft for the fourth year in a row. So that is very important, right, meaningful. And the position of Embraer in customer support also has being such that we have been able to grab a lot of attention and gradually also improve our client base. So, all-in-all, so we believe that we can see better results like going forward now.

The U.S. economy has, as we all know here, is going through a process with the new administration, which can but provide additional growth, right, in the market. So, we are seeing what Wall Street is thinking about this new administration. So, with stock market going up and the (32:24). And we know that business jet, Executive Jet is very much linked direct to both, GDP and stock markets. U.S. market is the largest market in the world for business jet, about 60% of the global market is within the United States. So, therefore, it's one more element that can help for this market to improve for now.

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

Thank you.

Okay. Our next question will come from the phone. Operator, can you open the line and introduce the question please?

**Operator**

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

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

Yes. Thank you very much for taking the call. So, if you look at 2018, do you feel you will be able to hold your commercial margins as you introduce production of the E2? And secondly, should we look for a lift in business jet margins, because I assume this year, your production will be down so that you can reduce your inventory of wide tails? Thank you.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Cai, can you repeat the first question please? The second is regarding the business jet margins, right?

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

So the first part of the question was, for margins next year, do you introduce, do you feel you will be able to hold them or are they likely to come down? [Technical Difficulty] (33:55) on business jet margins next year. Given that this, you have production down to reduce the wide tail, and I would guess that would not be an issue next year?

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

Yes, Cai. We're hearing very, very bad, but I - as long as I understood your question, the first piece was related to the margins for Commercial Aviation in whole in 2017. Yes, we think we can have, we can retain that as per the plan, primarily orders that we have before and we have like Paulo mentioned, the discipline in terms of cost that we'll be able - we think we'll be able to retain those margins for Commercial.

Regarding Executive Jets, definitely we expect to have a better margin, 2017. The last quarter of last year, although this is always the best quarter of the year, but you can see the improvement in the results which reflects what we mentioned before about to be more disciplined in terms of the deals, making sure we're not matching the others and that we have quality on each deal that we get into.

So we expect to see there an improvement of margins in the Executive Jets in 2017. If I'd missed somewhat - you can repeat please if we missed anything from the question.

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

Okay. We're going to try to reconnect Cai, and maybe we can move in the meantime for the next question also from the phone. Operator, can we have the next question from the phone please.

### **Operator**

Our next question comes from the line of Darryl Genovesi of UBS. Your line is now open.

### **Q - Darryl Genovesi** {BIO 20862546 <GO>}

Hi, guys. Thanks for the time. So your margins in the fourth quarter were up a lot relative to last year. Can you give us a sense how much of that is your cost cutting program flowing through, and how much more there is of that to come in 2018?

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

Yeah. I don't have - don't have the margins of fourth quarter breakdown...

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

Yes. Maybe, yeah, maybe you can give the details of the margin per business Darryl, thanks for the question. We had 12% EBIT margin, consolidated EBIT margin excluding non-recurring items, 14.8% on Commercial Aviation, 9.2% on Executive Jets, and 9% on Defense & Security. The cost cutting plan was larger towards the end of the third quarter,

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and we already capture, as I mentioned on the previous question from Turan, we already capture part of the \$200 million mission in the fourth quarter.

So it's - I think it's tough to quantify the percentage of the margin improvement that comes from cost cutting, but it's a combination of cost cutting. Our change out there in behave (37:18) on Executive Jets focusing more on profitability rather than volumes as we have already said. So it's a combination of things. So I don't know if Filippo and Paulo want to...

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

No, no, I just wanted to add that, it's important about the performance of the last quarter as you said, good margin. But this is not what this should replicate for other quarters, typically that's the strongest quarter. I think that in a yearly basis, as we indicated the guidance range, could be broken by our businesses (37:50) by low-double digit for Commercial and mid-single digit for Defense and for Executive. Therefore, on the blended basis, this will return to the 9% - in the 8% to 9% that we are expecting for the full year 2017.

### **Q - Darryl Genovesi** {BIO 20862546 <GO>}

Okay. Thank you. And then on free cash flow, based on your guidance today, for the \$150 million outflow in 2017 within the context of I think about \$400 million in development spending, would you expect that free cash flow number to turn positive in 2018?

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

No, it's still too early. Of course we don't give guidance for 2018 at this point, but as we already indicated, 2018 is a very - is a transition year for the E1 and E2 model. So again it's too early to see, to think about that in terms of our disclosure. But I don't think it's going to be - it can be better than that. As you know, in the recent years we're trying to be breakeven, because it's a very important phase of investment and the learning curve of a new model is always something that we'll have to go through. So if you have something, you take into account what we expect in terms of cash generation for the following years.

### **Q - Darryl Genovesi** {BIO 20862546 <GO>}

Okay. Thank you.

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

Okay. Maybe we can take a question from the audience now. If you have a question please just raise your hand.

Hi. (39:39) from Deutsche Bank. What is the spot rate you assume for the year?

### **A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

320.

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

Okay.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Between 310 to 320 which is more or less at the current level, that's our tax for 2017.

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

Very good, thank you.

Hello. This is (40:10) from Goldman Sachs. How much services is there in the margin guidance that you guys gave?

Maybe \$300 (40:24), so who knows.

Okay, fair enough.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Our guidance of course reflects, what - there are challenges on the guidance always, because that's the way we work. But we have to do something that we think it's going to be reasonable and achievable. So, I think there's a combination of what we see, because we have some orders already booked but there's still challenges to sell this year, which typically we have, not different than we have before. I think last year we had a lot of non-recurring items and lot of impacts on the company that affected the whole, the company, but taking that out I think the trend is to really be in a situation where we can really achieve those targets and challenge that we have, specially because we - we had this focus on the cost reduction. I think that will be reflecting. They have - the impact of the stronger currency is always a headwind, that we'll have to face this anyway. So I think that's the reason. Well, that we can - that's what we expect. There's no - I don't think its conservatory, I think it's realistic.

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

So just how much of contingency there is in this fund, because if you think about it, as you said, there is a lot of non-recurring that won't happen anymore and there is the cost cutting that should kick in already, or at least a good hard portion of it in 2017. So how much of the deals are contingency plans there might be embedded in this guidance so that we achieve the levels that you're talking about?

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

So I don't think we have much contingency to be accounted for in 2017. Let's say what we have in 2016 was more like a one-time impact. The KIPCO contingency that we have are related to in term of (42:11) airline, which (42:12) and this is diluted throughout the year, also other (42:17) contingencies that we always disclose, that's in the balance sheet. So there is nothing specific that we can anticipate in 2017.

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

Thank you.

Okay. So let's maybe take one more from the phone. Operator, can we take question from the phone please.

**Operator**

Our next question comes from the line of Alexandre Flacao (sic) [Alexandre Falcao] (42:38) of HSBC. Your line is now open.

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

Good afternoon, guys. My question is - my questions are regarding Defense. First, on the receivables front, how much we still have to receive from the government and where are we on the program in terms of the KC, and some other cases is going to - when it becomes operational, what happens in terms of the pre-operational expenses and how you guys are going to go out to the market? Whether it going to mean lower margins there?

And as Jackson pointed out in the last Embraer Day, that you expected to have almost 60% of the revenues on being dollar denominated, U.S. dollar denominated. Where are we on that, and what we expect, and what's the expectancy of margins for 2017 and specifically on Defense? Thank you.

**A - José Antônio de Almeida Filippo**

Okay, Alex. I'll try to see if I get all the questions. In terms of receivables from the government we end up 2016 with \$264 million in receivables, and that can be compared to for \$350 million in the end of 2015. So it's been following the schedule as we expected. The development of the program you have, this year is an important year. It's scheduled to enter into service in the first half of 2018, and this is going to be - the development program will stop and we start to build the series, the program. It is - as the contract of this sale of our customer today is the cost of over - recording through the cost.

So we will - I think we'll have through the development and the manufacturing of the aircraft will be recognized in the revenues, that could be seen in 2018 or as we're starting, maybe in the end of this year. And then there's going to be of course the learning curve of the program, which we don't anticipate any pre-op charges.

In terms of the revenues today still 90% of the revenues are Defense are reais denominated. And this will be changing when we have the (45:17) mostly related, then it will not be a big change in terms of the revenues shift into a dollar-denominated revenues, almost all of them.

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

Okay. Thank you. And if you can just – if there's bump up in the defense budget in the U.S. do you think there's opportunities specifically for the Super Tucano, is there any indication that you're going to see a recurring order there? Anything you can share? Thank you.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Yeah. Of course, we see we have the Super Tucano with U.S. Air Force in operation in Afghanistan. The information we have is that the U.S. Air Force is very happy with the performance of the aircraft. So, going forward now, of course, so we have to wait and see the opportunities that will arrive to us.

There are mainly information already on the press of the need for the U.S. to replace certain aircraft not only in military – and like the Super Tucano a replacement for the A-10 for an instance. But more recently also talked about jets, business jets for training like pilot training, so it's another opportunity also, but we will have to wait for additional information and see how we can move forward from here so it's early to say.

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

Thank you so much.

Can we take another question from the audience. Anyone?

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

Bruno from Santander. I have a follow-up question on the executive division. You have mentioned that going forward you intent to focus on profitability rather than on increasing deliveries. So volume is not in our main focus right now, but your guidance implies a similar level of deliveries, similar number of deliveries versus last year. So how should we look at it. How can you improve profitability, if you're not increasing the number of deliveries this year? Thank you.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

If we look at our guidance last year in February, our guidance were for 150 aircraft or so, business jet, so then in August, so (47:53) to 117, if I'm not mistaken. So it was a big adjustment.

**A - José Antônio de Almeida Filippo**

119.

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

119. So it was a big adjustment, all right. So what we are seeing now is that with this level, so we are able to improve our margins. And we already have a good indication from the fourth quarter, because from August, when we decided to drop the level of aircraft (48:25) in the markets, we closed many deals already from August to November, December, especially to November. And we could already see some improved in margins. So going forward now which this view that the markets can also improve a little bit from

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the bottom of 648 aircraft last year. So we believe we can keep this more or less the same number and still have (48:53) improvement.

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

Okay. So but what does this improvement in the fourth quarter come from, is it the market that is improving or is it something that Embraer specifically is doing?

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

Both. It was more (49:06) in terms of price, in terms of - I'm not putting too much pressure in market share. So, it was the combination of a cost reduction and a little improvement also in price of aircraft, small improvement in price of aircraft.

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

Thank you.

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

Anyone else from the audience with a question? Otherwise, we will move back to the phone. Operator, do you have questions on the phone?

**Operator**

We have a question from the line of Derek Spronck of RBC Capital Market. Your line is now open.

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

Okay. Thank you. Just turning back to Business Jets again, how is the mix right now between the Phenom and the Legacy 450/500. Are you getting the orders that you anticipated and the pricing on the Legacy? And when we look at 2017, how do you think the mix will be between those two aircraft types?

**A - Paulo Cesar de Souza e Silva** {BIO 17023173 <GO>}

So, as I said for the Phenom 300 it was the most delivered aircraft last year. The Legacy 450/500 it's a growing interest in these aircrafts now. So, we start to deliver back in 2015. We are now manufacturing, sampling both in the U.S., in our factory in Melbourne for the - we delivered the first one, Legacy 500 back in December at U.S. manufacturing in Melbourne. So, going forward now and we are seeing more and more interest in the Legacy 450/500. So, I do believe that 2017 will be a year that we will see a great interest in these aircrafts for that at least.

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

Okay. Just moving on quickly to the E175-E2, you think that the scope clause changes from the (51:30) to allow the higher weight aircraft on the regional jet side. What are your plans there. I mean if there aren't scope clause changes in the future, do you plan on manufacturing both the current generation E175 and the new E2 E175?



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**A - Paulo Cesar de Souza e Silva {BIO 17023173 <GO>}**

Well, the current E175 is a very efficient aircraft, no question about that. So if you look at the number of orders that we have got in the last year, so it's 80% of the market share versus the CRJ900.

So we do believe that with the modifications that we did in the wingtip and other improvements and getting a fuel burn reduction of about 6% that was crucial in order to get these orders. So we have then a very efficient E1. The difference to the E175-E2 is about another maybe 6% or so.

However, we have this scope clause in the U.S. So there is almost nothing that we can do to change the scope clause in the United States as a manufacturer, all right. So, it's really very challenging, even for the airline, it's quite a challenge to negotiate scope clause for this type of aircraft. However, the 76 market is not only in the U.S. so there is a markets also outside the U.S., and we have to - we have to be ready and pay attention for the competition that is developing also an efficient 76 seater like Mitsubishi for instance.

So going forward, so we can afford to monitor a little bit the U.S. market and continue with the E1, right. We have a good advantage in this regard, I'd say because we can have in the same line of a jet hybrid line, so we can manufacture both E1s and E2s in the same line with the same level of efficiency.

So for a while, right, so we can do that. And whenever, the scope clause change in the future, if it does, so we would be ready also to deliver the E2-E175. So we'll see how the market will develop, but in our view, so we are doing very well, both I think in this regard and we have decided to postpone one year, the E-175-E2 now it's 2021, which I think was a good thing to do since we have this scope clause topic in the U.S. now.

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

That's great color. If you were to manufacture both concurrently on a hybrid line, would it add - would it put any pressure on margins or how material would that cost be or would you be able to manage that?

**A - Paulo Cesar de Souza e Silva {BIO 17023173 <GO>}**

No. we're not anticipating pressure in margins. So we are - of course, we are not yet (55:04), but we are taking the necessary steps to be as efficient as we are nowadays. So we believe that we'll keep the same margins, at least.

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

Okay. Thanks very much.

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

Hi, (55:23) Can you comment on your cost cut, what percentage was allocated to Executive and what percentage was allocated to Commercial? And second question, in

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the past, if I'm not mistaken, you were using trading in the market for Executive segment. So how is this trading evolving right now, do you continue to do this as a market practice?

And also you mentioned about your inventories, were inventories for the Executive segment higher than usual or not, just to understand, if you're, sort of, change your strategy of carrying more of this aircraft in your inventories instead of selling them to third-party as a trading? Thank you.

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

Yeah. In terms of the allocation of cost, there is no specific allocation for that - the cost reduction applies specific for one division, most of the cost reduction was fixed cost, like the receivable and other things, normally it's allocated through the percentage of the revenues, so it's more like a distributional, the amount. The percentage of the revenue we should take that percentage rather than have specific. I won't say that to one of the - any specific business had more reduction than the other, because of the plan of reduction.

In terms of the inventories, we ended up with a little bit more of inventories in 2016 as we indicated because we decided to reduce the offer during the year but the carryover production would require us to have higher inventories we have as expected not more than what we expected, and this is going to be adjusted throughout 2017. I think, there's another question.

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

About...

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

In terms of trading, I got it.

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

Thank you.

Tradings yes, we still do, because it's a market demand but not at the same way. I think, it's part of the, what we said about the focus on the profitability and the result of it (57:33) results, so we can expect tradings but not as a basic assumption. I think, you have to analyze and there's a criteria now for us for accept the tradings, but it has to continuously be done because it's part of the business dynamics and the market dynamics. So we'll do but different than we did before, lower numbers definitely with more quality in terms of the way we approach the deal.

Okay. Any final question? No. Okay. I think, that's it. That concludes our 2016 earnings call. I want to thank you all that are attending by the phone, you can now disconnect. For those that are here we're going to do a short break, 15 minutes and then we're going to come back, we're seeing the video presentation of each one of our business units. Thank you.

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