

Q4 2010 Earnings Call

Company Participants

- Cynthia Benedetto, EVP Financial and CFO
- Frederico Curado, President and CEO

Other Participants

- Caio Dias, Analyst
- Ron Epstein, Analyst
- Seth Tennant, Analyst
- Stephen Trent, Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to the audio conference call that will reveal Embraer's Fourth Quarter 2010 results. Thank you for standing by. (Operator Instructions) As a reminder, this conference is being recorded and Webcasted at www.embraer.com.

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 the other markets where the Company is present. The words believes, may, will, estimates, continue, anticipates, intends, expects. And similar words are intended to identify forward-looking statements.

Embraer takes no obligation to update publicly or revise any forward-looking statements because of new information, future events, or other factors.

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

Participants on today's conference call are Mr. Frederico Curado, President and CEO; Ms. Cynthia Benedetto, Executive Vice President and CFO; Mr. Andre Gaia, Director of

Investor Relations; and Mr. Rodrigo (inaudible), Tax and Accounting Director.

I would now like to turn the conference over to Mr. Curado. Please, go ahead, sir.

Frederico Curado {BIO 2004589 <GO>}

Good morning. Thank you for your participation on our conference call here present in Sao Paulo and also through the internet.

We will discuss a little bit about our 2010 results. We will provide an outlook for 2011. And then, of course, we'll open the floor for questions.

Some highlights about 2010. Important is the fact that we did deliver all of our guidance projections -- either achieved or surpassed. We're going to go through them.

We registered earnings per share of almost BRL0.80 and earnings per ADS of \$1.8.

As far as commercial aviation, we had -- After two years of slow sales, we were able to get almost a one-to-one book to bill and with 97 new orders and 101 deliveries.

Our customer base, very importantly, was expanded further. We have E-jets now flying in 39 countries in 58 customers. So this is quite an improvement, taking the previous presence of Embraer. This obviously illustrates a very positive environment not only operatingly -- prospects for the E-jets but also for the liquidity and the financability of those assets.

We delivered 700 E-jets last year. The customer was British Airways. And we also improved our market share in the business jet market. As far as deliveries, we reached 19% market share last year with, of course, the ramp up of the Phenom 300. 145 jets, 19 large-cabin. And 126 small-cabin. Large-cabins are Legacys and Lineages. Small-cabins are Phenoms.

I think a landmark order from NetJets -- not only the size of the order but the importance, being NetJets is the largest corporate jet operators in the world, a very sophisticated customer, a very demanding customer. So 50 Phenom 300s for that customer.

And one more program that Embraer certified on time. The Legacy 650, which takes the range of the Legacy closer to 4,000 miles and new avionics, new interior features, through the north Atlantic -- business jets -- were certified on time -- all three aeronautical authorities -- last year in Brazil and Europe and earlier this year in the United States.

Defense also -- I think it was an important year for the solidness and sustainability of this business. We do see it as one of the potential growth avenues for Embraer in the mid; to long term. We had a successful outcome of the discussions country to country between Brazil and Portugal, the Czech Republic, Argentina, Chile. And Colombia for their

participation in the program, both industrially and also, of course, as an operator -- as acquiring the aircraft. Those LOIs obviously -- they have to be succeeded by specific agreements on both industrial and commercial sides in the next couple of years. But the intention is there. It's a very good start for the program.

We also had our first successful penetration in the Asian market as far as defense products, with eight Super Tucanos for Indonesia.

And, having in mind our long-term vision for this business, we created and separated a corporate unit to handle the defense business and expanded not only in terms of size but also in terms of broadness of our activity -- the range of our activity -- not only the Air Force but also start looking into opportunities with the Army, with Navy, with homeland security types of applications. C4I -- the two major events coming to Brazil. So we see there is growth there. And we want to address that growth in a very dedicated and specific manner.

We celebrated four ten-year anniversaries last year.

As far as sites, we had our Gavião Peixoto site, which, in ten years, grew from greenfield to 1,600 or 1,700 people and all of our test flights, the fabrication of our 190 wings. And all the military programs there.

We also celebrated ten years of our presence in China and in Singapore.

And ten years of our listing in New York Stock Exchange as well. We were honored with closing the bell last October, marking the ten years of our shares floating in New York.

As far as governance and as far as people, which is our number-one value, for the second time-- for the second year in a row, we were included by two distinguished magazines in Brazil with specific and totally independent assessments, one of them including working with the Great Place to Work Institutes as one of the best Brazilian companies to work for. So this is a great pride for us, taking the size of Embraer and the size of our blue-collar workforce.

We were again part -- selected to be part of the ISE, the index of the Bovespa, the São Paulo stock exchange, sustainability index. Actually, we have been part of that index since the index was created several years ago. And we were back to be included in the Dow Jones sustainability index with a gold class. So that was a particularly rewarding achievement for all of us for our financial area but also for our -- the whole Company, as far as the initiatives also that we have on the social and environmental fronts.

And preparing for the vision that we have that Embraer can expand beyond just the current scope is, we have dropped the whole description of the acronym Embraer, Empresa Brasileira de Aeronáutica. And shortened it to Embraer late last year. So, with that, we also opened the scope of the Company -- the business scope that, as I said, on the defense area may also address other areas than aeronautics specifically but also

gives us an opportunity to investigate a potential participation on the energy business. So those two elements are now part of our social objectives.

As we had indicated, we saw a stable 2010. Our guidance was \$5 billion in the quarter. We surpassed that a little bit. So, fundamentally, the same level of revenues, the same level of activities that we had in 2009, which, given the circumstances, was, I think, a positive result for us.

As far as deliveries, that achievement and that surpassing of the revenues came because, of course, we had a few more deliveries than forecasted. As you can see, in blue, you have the commercial jets; in yellow, the large-cabin business jets; and, in green, the small-cabin business jets.

By the way, more and more, it will be less, I think -- it will be less meaningful to talk about deliveries and, I think, be more meaningful to talk about revenues because now we really have such a broad range of products that a Phenom 100, a \$3.8-million aircraft vis-a-vis a Lineage 1000, a \$50-million-plus aircraft, or 190, a \$30-million-plus aircraft, really creates, I think, a tough modeling for delivery versus revenue. And we are giving guidance for revenue anyway by business area.

Well, our backlog had a little decrease vis-a-vis 2009. But, if we break down 2010 into quarters, you see that the second half of last year we already stabilized our backlog in the \$15.5 billion. So this is roughly worth three years of production, obviously. This is not solid. We have some programs that go away beyond three years. But, again, I think the worst is behind us. And we were able to flatten out and now, hopefully, to increase our backlog again to higher levels. About half of that backlog is commercial aircraft, about 20% is defense and 30% business jets.

If you take the breakdown of our revenues in the last three years, there's a clear -- all the directions of diversification -- I think they show up there. We have been able to grow the business jet and defense businesses in the mix of Embraer total revenues.

And, also, even more importantly, the geographical diversification -- Brazil, from a simple 4% three years ago, it is now 13%. Obviously, there is a reduction in total revenue that helps that calculation. But it is growing. So our presence in Brazil, our presence in Latin America -- if you sum both, Brazil and Latin America, 28%. It is the second-largest market for Embraer last year -- the second-largest destination of our products and services.

As far as financial results, we had a strong quarter. That took, again, to achieve our guidance as far as revenues. It's \$5.36 billion. Stable gross margin. And I have to make a remark that that gross margin, of course, had some strong headwinds as far as the Brazilian currency, which was offset by productivity and a lot of investments that we have been doing and continue to do in our quality, productivity, motivation of our labor to face those challenges.

We pretty much kept G&A flat; again, despite the strong valuation of the real. Commercial expenses, selling expenses, they were up due to several factors but, fundamentally, to

increasing the infrastructure to support our new programs in the markets and, most importantly, on the business jet side. As we deliver a hundred or a hundred-plus aircraft per year, we have, of course, to invest in spare parts, invest in the certification of repair stations as far as people. And, obviously, warranty. So this is the fundamental origin of those seller expenses.

In US GAAP and IFRS, the numbers are very, very similar. And they are reflected there.

As you know, from this call forward, we will concentrate only on IFRS, which is the legal system in Brazil and is also the one accepted in the United States. That's why we're trying to give you that comparison. So you can take that reference forward and have a seamless transition, hopefully.

As far as operating margin, we basically achieved our guidance, which was 7.25%. We reached 7.3%, a little bit -- 0.05% higher. Again, a strong quarter, last quarter of last year. And, as I said, despite all the challenges coming from the currency and the valuation also of the Brazilian -- not the valuation but the increasing costs of the Brazilian labor, which has been growing above inflation, above just the real appreciation. So we have the combination of a strong real and real increases in reais. So that has been the challenge on not only Embraer but all Brazilian exporters.

As far as EBITDA, there is -- yes, there is a reasonable difference between US GAAP and IFRS. But we achieved our guidance and surpassed it. And I think it was a direct consequence of our operating results.

Net income. If we take IFRS, that decrease has to do with the fact that Brazil still has a separate legislation for income tax calculation, which makes all of our lives difficult as far as forecasting net results. Even for us, it's difficult. In US GAAP, you have a more predictable -- actually, it's also influenced positive on the 6404[ph]. Anyway, apples to apples, we had an increase in our bottom line this year, 6.5%. I think it was a positive result for us.

The earnings per share and the payout as far as dividends. Historically, we have been distributing 50% of our profit as dividends or interest on capital. During the crisis in 2009, deliberately, we distributed the minimum that the Brazilian law requires, which is 25%, to preserve cash. And, as we feel comfortable now, we are going back. Around 35% is what we have distributed last year. And this is roughly, I'd say, a number that we consider a good average. We have no policy for dividend distributions. It's a decision quarter by quarter by the board of directors. But that increase reflects a higher comfort as far as our cash position vis-a-vis the future demands.

Positive cash flow. Our free cash flow was \$287 million last year. So it was good. We had a challenge the First Quarter and the third as well. But the two strong quarters in the second and fourth gave us a positive figure yearend.

That's a nice story that Cynthia can tell you about. We have a strong cash position. And our indebtedness has long-term maturity. So it's a very comfortable place to be as far as

indebtedness and cash position. We know the importance of having a strong balance sheet in a cyclical business such as ours. And that conservativeness will always be present in our minds, either because I have to face investments forward or because I have to be prepared to face any unknowns from a terrorist attack in 2001, from a volcano in Iceland, from now the situation in the Middle East. So companies that leverage their balance sheets in our business, they are really taking a risk which we are not prepared to take. That's why we keep a conservative position as far as cash.

And, as a closing comment, talking about our outlook for 2011, a bit of growth as far as revenues, about 5% -- not a brilliant growth. But that is a reflect that both businesses, defense and business jets, are relatively flat. And the commercial jets do see a bit of upside, although, again, not stellar. So we see a 5% growth in our revenues next year; that revenue, in spite of the continuous appreciation of the real. As you know, the real has appreciated in 2011 already.

We expect to translate that growth also into margin. So we are raising 7% in our EBIT and the margins roughly the same -- a little bit, 7.5%. EBITDA stable at \$610 million.

These are our outlook for 2011.

Investments I think is an important -- We have separated research and development because, in US GAAP, they are all expensed. In IFRS, they are not. The research, which is pretty competitive expenditures, they are expensed. The development, which is basically related to new program developments, they are deferred and then amortized in the COGS. So I think to help you all to model the way you follow the Company, it's fundamental that, from now on, we have to separate that. So you can have a clear picture. Obviously, from now on, you must look at our cash flow also to evaluate our expenses of R&D. In US GAAP, you could pretty much look at the financial statements. But now you have to be careful because those \$210 million -- they'll not be expensed. They will be deferred for future amortization.

And CapEx. As, certainly, many of you recall, for the last two years, we have been postponing what we could postpone without jeopardizing our programs. It is now time to really pick it up and catch up as far as those investments. We have Melbourne, which will deliver the first jets before yearend. We have the two factories in Portugal, which we produce the first (inaudible) in the first half of next year. And we have tooling and other equipment for the Legacy 450 and 500. So the CapEx bill will go up this year to levels which are compatible to what we have had in the past, as you can see in that figure. So it's a significant year for investment for us; overall, about \$500 million of investment next year.

With that, I will close the presentation and open the floor and also the people who are in the call for questions. We'd be very pleased to answer them. Thank you.

Questions And Answers

Operator

(Operator Instructions) Joe Nadol, J.P. Morgan.

Q - Seth Tennant {BIO 2497049 <GO>}

It's actually Seth on for Joe this morning. A couple of questions. First of all, the guidance for EBIT, at \$420 million, I was wondering, first of all, if you could talk about the inventory adjustment charge that you took in the Fourth Quarter. And then, if you add that charge back, you're actually forecasting that EBIT is going to be coming down in 2011. I wonder if maybe you could quantify a little bit what's causing that decline and how much of it results -- is from the appreciation of the real, from the increase in your labor cost, from maybe from any changes in mix with defense coming down.

A - Frederico Curado {BIO 2004589 <GO>}

You were coming across quite tough to understand. Maybe the natives -- they could understand you better. If I got your question right-- This is Joe[ph]. Right?

Joe, if I got the question right, when we gave the guidance of 7.25%, we had the expectation that we could have to make some sort of a write-off or provision in this quarter. We did not know this was after -- during the last quarter, actually. So, no. We were not-- We had no idea of having a higher operating margin in 2011, which was reduced because this impact was earlier than forecasted. No. This is not the case. It was the other way around, actually. When we thought about 7.25%, we kind of thought that, among the potential impacts of some nonrecurring events to our results could happen -- if would happen, would happen in 2010, as they did actually.

I'm not sure I answered your question. But that's what I understood from what you asked.

Q - Seth Tennant {BIO 2497049 <GO>}

Okay. That's helpful. Thank you.

If I could ask one follow-up, it's just about business jets. If you could comment on the demand environment -- you mentioned book to bill remaining below one. You've forecasted decline in the Phenom deliveries for this year. And I think that -- I know the environment is still difficult. But I think maybe the sentiment had been about maybe some order activity across the industry improving in 2011 and maybe eventually leading to higher deliveries in 2012. It looks like you're not really expecting to see all that much strength in the way of orders. Maybe, if you could, comment on that.

A - Frederico Curado {BIO 2004589 <GO>}

If we look backwards and see the profile of our growth in the business jets market, we had some step functions. And those step functions -- they were a direct result of the certification and entering to service of new products.

FINAL

In the last few years, we have had a new certification -- a new certified program, a new certified product coming to the market every year. That has really given us this very aggressive, compounded average growth rate in the last few years. In 2011, we do not have that. Basically, all the airplanes are already certified.

As you see, despite the fact that we have less airplanes to be delivered in 2011, the revenues are pretty much at the same level because the product mix will be richer than it was last year. Translating what I'm saying, less Phenom 100s and more Phenom 300s and Legacys.

And we see ahead organic growth -- not very steep growth but some organic growth in the market next year, in 2012. But, again, in '13/'14, as we introduce the Legacy 450 and Legacy 500 into the market, we'll have another step function in our revenues and our market share because we'll be addressing two new segments in which we have no product today. So, between today and the entrance to serve those to new jets, basically, we will follow organic growth.

This is roughly the helicopter view of the business.

Q - Seth Tennant {BIO 2497049 <GO>}

Okay. Thanks very much.

Operator

Stephen Trent, Citigroup.

Q - Stephen Trent {BIO 5581382 <GO>}

Just two questions from me, if I may. I know you're somewhat deemphasizing jet deliveries now versus the past. Just curious. In terms of the commercial jet guidance for 2011 versus what you did in 2010, have you recently adjusted your thinking, given the turmoil that we're seeing in world markets and geopolitical events, the stuff in Libya, the terrible tragedy in Japan? Have you recently adjusted your thinking in terms of putting out this guidance? That's my first question.

A - Frederico Curado {BIO 2004589 <GO>}

Japan. First of all, let's talk about Japan. We have just a few orders outstanding in our backlog for Japan. Our preliminary analysis is that there will be no impact to that. And, actually, we just delivered one 170 for Japan Airlines.

And, on the supply chain side, maybe our most relevant supplier in Japan is Kawasaki. They were not hit directly by the tragedy of either the earthquake or the tsunami.

So the concern is to understand. And I think nobody at this stage really knows that, not even them, what is the duration and what is the depth of the impact to Japan as a whole, the economy.

Bloomberg Transcript

So the first analysis is no direct impact. And we have to wait maybe probably a few more weeks to fully understand if maybe sub-tier suppliers who have some indirect impact on our major supplier and, therefore, to ourselves.

And this obviously is no particular position of Embraer; it's the whole industry. Obviously, for example, Boeing is much more exposed to Japan than we are. So I think it's an industry concern, not only ours.

Now to your question about the guidance and if it's more or less conservative vis-a-vis Libya. No. We did take into account that the oil prices will potentially reduce the profitability of the airlines. IATA number calls for some 40%-plus reduction from the \$16 billion forecasted for this year to something like \$9 billion or so next year. So that, of course, gives us a bit of conservatism as far as global demand. We have 100% of our production in 2011 already sold and a very, I would say, comfortable position as far as sales financed for that amount of airplanes, as well, already taken care of or, at least, in a very good perspective.

So I would say there's no specific impact from Libya or from Japan. There is an overall caution vis-a-vis the air traffic -- the commercial traffic coming from higher oil prices, which potentially will impact profitability and demand on the airlines side.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Very clear. Thanks, Freddie. Just one more question. And I'll let somebody else ask a question.

Just wanted to get your thoughts on the competitive environment. Airbus is doing the NEO. Your Canadian rival seems to continue advancing on the C series. Boeing's telegraphing that they're going to clean sheet. Any update on whether you're going to clean sheet?

And then, on the business jet side, at least, some indication that Cessna is looking to retrench. I just wanted to get your thoughts on that.

That's it for me. I'll let somebody else ask a question.

A - Frederico Curado {BIO 2004589 <GO>}

Those are two questions, Stephen.

Q - Stephen Trent {BIO 5581382 <GO>}

Sorry. I cheated.

A - Frederico Curado {BIO 2004589 <GO>}

Well, let's first address the commercial side. The NEO has been -- has already captured orders. At least for me, it's clear that the NEO will actually pick up from the existing 320s.

So it's really a continuation of the 320 heritage, a very successful program. And that view, in my perspective, increases the longevity of the 320 family years down the road.

I see a direct impact to the C series. I think the new -- some of the successes that have been announced by Airbus somehow were customers were being worked to address by Bombardier in the C series. So I think the NEO does not help the C series case.

Boeing, I think, more and more talks openly about a brand-new design, which, in my humble perspective, makes a lot of sense to have something, as their engineering is probably going to be less and less loaded with the 787 and the 47-8. You have that amount of resources available. So a clean-sheet design makes sense.

And we are waiting. As far as Embraer, we are waiting exactly to understand where Boeing is going to define whether or not we engage in the development of a new, larger aircraft -- when I say larger, typically, a five-abreast aircraft -- or if we keep ourselves focused in the existing segments by revamping the E-jets at this stage.

To revamp the E-jets at this stage is something which I think is premature because the airplane is still state of the art. Sales are a testimony of what I'm saying. Sales have come back. And we had a good start this year with Alitalia and other orders that we have had already.

So I do not feel pressed at all about re-engining or redesigning the E-jets. They are very competitive aircrafts.

So what we really should focus is -- is there an opportunity for Embraer to increase its participation in the market by coming to the next segment in the, let's say, 130 seats or so segment with a five-abreast aircraft? I think that the final piece of this moving puzzle, which I have been talking about for the last three, four, for five years, looks like it's going to be fixed within the next few months by Boeing. And then we'll have a decision.

So, yes, I do anticipate Embraer making a decision on that investment before yearend as a result of the competitive landscape.

Now, we have so far -- What have we done this year? Not only we have, let's say, a reasonably comfortable product -- backlog competitive product; we have a solid cash position, a solid economic position. And we have also during those last four or five years invested significantly in technological development. If we decide to go ahead, we will be ready as far as technology. We will be ready as far as industrial capability. We will be ready as far as the ability to fund the program and with the correct productivity and labor skills to address that.

Now, on the business jet side, the market's clearly lagging behind the airline market. I did read Cessna's intention to develop a brand-new aircraft.

FINAL

Bloomberg Transcript

FINAL

Pragmatically, what I see is that -- I think Embraer seized a very nice opportunity of bringing to the business jet markets in the last five years something new, which was something like having an airline design aircraft type to a market where reliability was not as important as it is on the airline side and bring some revolutionary products -- the Phenom 100, the 300, the new Legacys.

I do expect reaction. I don't think that a company like Cessna with almost 90 years of experience and a tremendous brand and capabilities would just sit idle. So I think this market will be more competitive. The market will be more -- Let's say I think the superiority of our products today, over time, will be challenged by competent people like Cessna. This is clear for us. And we are prepared to that new scenario.

We never thought we would have the ability to bring products to the market which were way superior to the existing ones. This gap tends to close the next several years. But, again, we'll keep investing and be prepared to try to keep the leadership in the segments where we are.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay. Very clear. Thank you, Freddie, for the explanation. I'll let somebody else ask a question.

Operator

(Operator Instructions)

Q - Caio Dias {BIO 21849043 <GO>}

I have two questions. The first one is -- What is the FX assumption you use when defining the operating margin guidance for this year, the 7.5%?

And the second one is related to the off-balance-sheet exposure you have deriving from the residual value and financial guarantees? Now that we are going through a scenario where we have a high oil price, there might be some pressure for the 50-seaters operators to ground the smaller aircraft. Do you believe that this could increase the risk of Embraer being exercised in one of these guarantees? Or do you believe that the scenario is very comfortable; you don't see any risk on this front?

A - Cynthia Benedetto {BIO 17063151 <GO>}

The average rate we assumed was BRL1.70. And, regarding the (inaudible), do you want to respond?

A - Frederico Curado {BIO 2004589 <GO>}

Yes. The oil price tends to affect 50-seater operations -- not only jets but also turbo props. I don't see the situation today worse than it was maybe three years ago, when oil was peaking to \$120 or so.

FINAL

And the customers -- the large fleets of our 50-seater jets are with companies such as American Airlines and, now, Continental/United. And Delta. So it will -- Unless we have a scenario where there are bankruptcies again, which I don't think is on the radar today, I do not see a particular risk for airlines going down and, as a consequence, having 145s not being -- the debt not being serviced and, eventually, Embraer being called upon warranties.

Parallel to that, we are working -- we're investing. We keep investing in the aftermarket of the 145. The 145 is retaining a higher residual value than its competitors. Recently, we announced we were very fortunate to engage one of the most senior executives in the industry exactly to integrate the whole sales/finance asset management as far as our use of the aircraft and also the interface with the leasing companies to make it even more solid. So we never took the eye off the ball of the 145. Although there are no new aircraft - - Actually, we have -- On the business jet side, we just sold a few (inaudible) 145s, which will be produced in 2011. So the lines are still open (inaudible). In spite of the very slow new sales, we never took the eye off the ball of the 145 as an important asset for us, for the people financing the assets. And for the airlines using it.

So the answer -- I do not want to sound too optimistic. But, realistically, I think we are well covered.

Q - Caio Dias {BIO 21849043 <GO>}

Just one follow-up question. I remember a couple of years ago Mesa, which is one -- a major operator of the ERJ 145 -- they were going through -- they were facing some liquidity problems. What is Mesa's current situation nowadays? I admit I have not followed their case.

A - Cynthia Benedetto {BIO 17063151 <GO>}

Mesa bankrupt. And, because of that, we create in January 2009 a provision in our balance sheet of \$100 million. Part of this provision has been materialized. We have cashed out part of this provision. And we still have remaining \$60 million as a provision for that situation on our balance sheet.

The situation is evolving. We are analyzing. We do not have the close of all the aircraft involved. And we are following the situation as we'd be required.

Q - Caio Dias {BIO 21849043 <GO>}

Okay. Thank you, very much.

A - Frederico Curado {BIO 2004589 <GO>}

Mesa (inaudible) operation (inaudible) some of their partners. They're no longer any Embraer aircraft.

Q - Unidentified Participant

Thank you. Just a quick clarification of two points. The 145, you said, is holding up better in value than its competitors. Did you say it's because there's a larger market share. And you're backing it up financially? Is that why the value is holding up?

A - Frederico Curado {BIO 2004589 <GO>}

No. The market share is actually a little bit less. And we're not backing up it financially. What we are -- We are investing in the secondary market, not throwing money away. We are investing in making sure that -- We have a portfolio of -- I do not know how many airplanes we have in our portfolio today -- maybe 30, 40, or so. But customer support, spare parts, supporting airline lessors or moving airplanes from one continent to the other, service bulletins, trying to make documentation as easy as we can -- But, also, what I have not mentioned, the actual machine -- the actual airplane is aging better than its competitors. That helps a lot too.

Q - Unidentified Participant

Okay. The other thing I wanted to clarify -- I thought I heard you earlier say that new businesses -- you were looking at maybe getting into the energy business. Did I hear that right? Is that something that you're seriously considering?

A - Frederico Curado {BIO 2004589 <GO>}

You did. When we opened our social objectives to a broader scope on the defense area, Embraer was only aerospace. Our solid object would confine us too aerospace. We opened that to defense and security with no boundaries.

And, also, we add energy. Why have we added? Because, of course, we're thinking about it. We do not have a business case yet for investments. And we will be very, very cautious to make an investment on that.

We're not trying to shy away or stay away from the aerospace sector. This is our main business. Our main business is commercial jets. We remain in big, commercial jets, certainly in my lifetime -- in my, at least, professional lifetime. So it's not that.

The question is how to find new avenues for growth and also to add some neutrality to the driving parameters of the cyclical behavior of the business jets and commercial jets -- how to bring some stability to our operations, leveraging out our core competencies. This is what we're doing. Of course, I have people fulltime investigating opportunities. Brazil has an opportunity -- has a need to grow as far as infrastructure. And strongly, in the next ten years. There will be opportunities on the energy sector, for sure, especially renewable energy sources.

Can we participate of that? Can't be sure now. But we're working hard to find a way to participate. Beyond that would be speculation. But we are dedicating resources -- small ones. But senior people and resources to investigate that.

Q - Ron Epstein {BIO 1868102 <GO>}

Two questions for you. One, Bombardier had, I guess, a strategic framework announcement with the Chinese. Two days ago, they announced where they were talking about possibly selling the C series and the C-919 together. It would give, I guess, jointly, 110; to 180-seat offering. What impact do you think that will have on Embraer? And maybe more broadly, what impact do you think that could have on the industry? Kind of what I'm thinking is -- could you see Boeing and Mitsubishi join together. And then that would -- What would that mean for Embraer?

A - Frederico Curado {BIO 2004589 <GO>}

Good morning, Ron. I think it's a very important development for the industry, what happens, although, in the short term, I could not understand some of the statements.

The C series is way down the road as far as development. And the C-919 is starting now. They're in the pre-design phase. Reading the -- I read this morning everything I could read about his news. It is not clear for me how they will achieve the level of commonality, integration they are talking about. So either the C series has to be redesigned and probably slowed down to wait for the C-919 to catch up and then somehow adapt it to the C-919 or the other way around. Or the Chinese will basically adopt the architecture and the fundamental systems design and supplier choice that it has already formalized. So this is a bit fuzzy for me.

But, taking now a longer-term perspective, I think this is a very important development. It shows or suggests that Bombardier is looking for some more solidness to its program and to its business, actually, the commercial aircraft business. So that may be a way for Bombardier to stay in the business or stay in a stronger way. And, certainly, you catalyze the Chinese learning curve; that's for sure.

So I think, if this really materializes into, let's say, a marriage -- this engagement becomes a full marriage in whichever form, either program, or even, why not, to think about a stock holding, I don't know -- it's pretty open. I see a clear upside for the Chinese as far as accelerating their learning curve.

And, for Bombardier, it's hard to say. It's a tough call, I guess, for them, because it's a call where you're basically leaving the full indebtedness to be teaming up with a partner in the long run. So I feel they're very relevant. And I think that has potential impact, again, not tomorrow but midterm and long term, to Boeing, to Airbus, to Embraer.

Is that going to trigger something else? Hard to say at this stage. This is like 24 hours only. I don't think Boeing -- I don't see Boeing reacting, going after Mitsubishi, because of that. I think Boeing has sufficient power and brains and all to define their own destinies. But I think this certainly is an element which will be, let's say, more highlighted in the industrial air -- especially in our scenario, for sure. The impact to Embraer is hard to tell at this stage.

The thing I can probably be a bit assertive about today is that we do not contemplate any architectural wear. Embraer will be a sub-supplier, or sub-tier, or tier 0.5, or a major risk-sharing partner. We see ourselves as independent and fighting for the leadership in the segments where we are. So we may decide not to engage in new segments. But to

where we are acting, we want to stay independent with our own capability. We do not want to relinquish our ability to address the customers. This is clearly our strategy today.

Q - Ron Epstein {BIO 1868102 <GO>}

Maybe just one follow-on question. When you look at the US fleet of regional jets, the 145s -- for example, at ExpressJet, there's a lot of aircraft that are going to come off lease in 2016, 2017. And 2018. What do you expect to happen to those aircraft? And what do you expect to happen to the US regional fleet?

A - Frederico Curado {BIO 2004589 <GO>}

I think it's inevitable that will happen. Those assets will be significantly depreciated. So I think it will fundamentally depend on oil prices. The oil are high. Even with a very low asset value, I see many of those airplanes leaving the United States and going to secondary markets. Today, if you ask for today, believe it or not, there is no available 145s for the secondary market. There is demands of two and threes, in places like Africa, eastern Europe, Brazil. And other secondary markets.

But the volume, I think, will be significant. So, if oil is very high, we may have kind of -- how do you say it? -- a glut all of a sudden in three or four years' time, hundreds of airplanes coming simultaneously with both CRJs and ERJs, which may create some difficulty to replace them in an orderly way, which we have been able to do so far.

Oil stays where it is now, I think there's still some case. CRJs[ph] being flown in the United States is not different from if the asset value is really low or zero of the cost -- or close to zero fully depreciated,. There may be a case for some utilization yet. And the cost per trip is still an event that is advantageous vis-a-vis larger aircraft.

Q - Unidentified Participant

I just wanted to try the business jet question again, recognizing your comments that revenue is becoming more important in units. The large unit decline in Phenoms is still surprising to us, I think, particularly given the market is getting a little better. You are taking share of a very large backlog. We were surprised to see that. How much of it is just the market is slower than some had been thinking? Or how much of it is -- you know, because it's the 100, Cessna is saying Mustang will be down significantly as well in '11. Is that very low end of the market just fully saturated at this point in the lifecycle of that program. And is that really the explanation?

A - Frederico Curado {BIO 2004589 <GO>}

I think they're very fair points. It's no secret to anybody that the business jet market has been much more hit, let's say, in the lower end than the upper end. So all aircraft (inaudible) that size are reducing its quantity. You just mentioned the Mustang. And the Phenom 100s is the same thing.

And then your question about the backlog. I think it's a very correct question. Our backlog was built in the good years. So that backlog stretches out many years down the road.

FINAL

What happens is, if people cancel orders or defer, we have -- for example, we have challenges. We have a few Phenom 100s to be sold for this year yet. And we do not know the cancellation until it's 18 months before delivery. That's when they have to put another pre-delivery payment.

So far, we have been very successful in bringing upwards -- in bringing people who have ordered down the road to take airplanes earlier. But this is a challenge. It's a daily challenge (inaudible) with cancelations.

The Phenom backlog stretches out probably three or four years down the road in a significant way and not necessarily will you be -- clearly, we are not able to keep a high production rate just bringing up customers which have deliveries down the road. So, in the current environment, many people are saying -- well, I'm not in a position to take the airplane today. But I do not want to relinquish my order. I want to wait the year and a half or two years that I do have in my contract. So we see that today.

So I think it's a combination of lower demands on the small ends of the market and also the profile of our backlog, which has this characteristic. So we prefer to reduce the production rate of the Phenom 100 to reflect that and have less pressure in making crazy deals just to bring people up and try to keep it more stable and always keeping in mind that the value of the Phenom 100 is significantly less. It's less than half of a Phenom 300. And it's a fraction of a Legacy. So we really focus on more of the quality of the revenue rather than engage in an exercise to keep the production rate at a certain level, which would require, really, some aggressive commercial attitudes to fill the gaps.

Q - Unidentified Participant

So you still have a decent amount of deferral activity. And you're still having to kind of shuffle positions in the backlog a decent amount at this point.

A - Frederico Curado {BIO 2004589 <GO>}

Yes. Absolutely.

Q - Unidentified Participant

I also wanted to follow up --

A - Frederico Curado {BIO 2004589 <GO>}

On the 100.

Q - Unidentified Participant

Yes. Okay.

I also wanted to follow up on the margin question that was asked earlier, which was that, if you add back the \$62-million charge, I think you guys would have done about 8.5% operating for the year. So you are effectively guiding to 100 basis points of margin

Bloomberg Transcript

compression in the underlying business, excluding that charge, which, given you're not getting that much volume and you have FX and you have labor going against you, I guess, isn't too surprising.

But, for those of us who were with you yesterday, we saw the COO's presentation and all the changes that have been made there. And we saw the factories that looked particularly streamlined and efficient.

So, once you're getting better volume beyond '11, how do you think about what the ultimate margin expansion capability of this Company is, given all those changes you made?

A - Frederico Curado {BIO 2004589 <GO>}

I think I could understand what you're saying. Just to comment on the 100 basis points, maybe your calculation is not -- qualitatively, you are right. And I agree with you. Quantitatively, you have to take into account that our gross margin has been affected by amortization of previous investments in IFRS, which would not be the case in US GAAP. So the comparison is not directly subtract that difference.

But, yes, we have cost pressure. This cost pressure is not only -- it's a double-dip headwind in the sense that you have the real appreciating vis-a-vis the dollar. But, also, the wages in Brazil. They are growing in reais. Last year -- I'll give you the number. Last year -- not last year -- we are now in the perspective of having some 10%-plus of higher costs in our labor in Brazil, all things considered. We have been able -- and the numbers that we are forecasting here, they show an aggressive response as far as productivity and as far as automation. But it is very hard in an industry like ours with no pricing flexibility to absorb 10% in a year.

So I agree that the outlook in 2011 is not stellar. It's not brilliant. I think it's realistic. And it actually has challenge behind it. And you have seen (inaudible) how we responding to those challenges -- fiscally, what we are doing. But I remain optimistic about what I just said in the final part of your question. As soon as you can have some markets perspective, some volume perspective, this thing will have a leveraging factor that will really push Embraer to better results.

The tough thing is we have only a 5% increase, which is market driven. It's not industrially driven at all. We have capacity to do much more than that. We did more than that in the past.

So you have a market which is still not fully recovered and headwinds like what I just mentioned. 10% in labor in one year, it's a lot. But we're not crying. We're not complaining. We are working hard. And, normally, you have better results in 2010. But I fully understand your frustration, if you will.

But it does not mean any, let's say, change in our attitude to improve the capacity of this Company and the productivity. Quite the contrary. It's just a challenge higher than it was

last year. And, of course, we'll work to beat those numbers. Of course. But I think, at this stage, it would not be correct to outlook something higher than that.

Q - Unidentified Participant

That's very helpful. Thank you, very much.

On the regional jet side, you're holding deliveries flat for next year. But you're sitting on about a 2.5-year backlog, not counting year to date orders. In the past, this has been kind of the area where you've ramped up production on the commercial side. So, given that you're holding it flat for next year, are you assuming a new -- what would be a new, healthy amount of backlog? Or are you looking at your backlog and saying there's some potential regional jet weakness given fuel cost? Why is that not going up from 100[ph]?

A - Frederico Curado {BIO 2004589 <GO>}

No. We expect to have a book to bill of at least one in 2011. So we definitely -- Today, we definitely see 2012 better than 2011. How much better? Too early to tell.

I can tell you this. We can ramp up our production in a relatively short time. Embraer has no constraints. Our infrastructure is for 15 airplanes a month with 180 airplanes a year. That's what we can do. But, of course, the supply chain has to come with that. So we are producing a hundred and a few airplanes a year. So we still have a lot of availability. It will be market driven.

So far, it's positive; as I said, a good start in the year. Of course, it would be premature for me to say, well, 2012 is going to be a real inflection upwards. Hopefully, it is. Of course, our sales guys are working hard to that. If we have the perspective of significantly changing production rates, we will for sure. And that does not interfere in any of what I have said about new programs. This is all parallel. Actually, this solidifies the path toward the new program.

Q - Unidentified Participant

Okay. And then one other question. Just talking about new programs, particularly on the biz jet side, can you just give us a quick update on the 450 and 500 and what the orders are looking like and also touch upon the KC-390 on the defense side?

A - Frederico Curado {BIO 2004589 <GO>}

The 450 and 500 -- they are going on time. We have a lot of work already way down the road as far as simulating the aircraft. We have full rigs. Actually, we have a full engineering simulation. We can fly the 500 in a simulator -- not a full-motion simulator but an engineering simulator.

So as far as investing in the quality of the design, I think it's probably a program that will give us smoother entry into service than previous programs. So it's okay. We have the classical challenge of some suppliers a little bit late and things like this. But, overall, the program is going quite well.

FINAL

I don't think we are devoting sales of the 500. Not many orders, I can tell you, because, of course, an airplane will come into service in a few years. The market today is not in the mood of committing. We have a backlog already. So nobody today would commit to an airplane -- to get it in five or six years ahead of time. There's no reason why you should do that.

The 390. Brazil obviously is overheating. And Brazil's inflation is creeping up. So the President of Brazil, very correctly so, has engaged in an exercise to control public expenditure -- the government expenditure. Whether or not this will have a direct impact to our program is not clear yet. Rumor is that it will. But we have not received any direct communication or amendment or anything like that.

Historically, every year, we have budgets approved. And there's a mechanism in Brazil which sounds silly. But it's true. The budget's approved by congress. But then the treasury -- the secretary of treasury -- the treasurer, they really kind of say -- okay, this is approved. But I'm holding part of that as a safety margin. This is not new. It's been happening all the years. And this thing -- The affected money[ph] ó gets released along the years.

So I don't see 2011 in a radically different way than I saw the last few years.

And I kind of believe the KC-390, because it has its own accounts, is not like procurement of the Air Force. It has a specific line in the budget. I kind of believe that everybody is aware of the importance of that program not only for us but for Brazil. At this stage, I do not expect to have a major hit to the program. And we'll keep going. As far as we do not receive any amendment or any slowdown in the program, we'll keep going. And they are current, by the way. And we also have other programs. So, overall --

Q - Unidentified Participant

I have two questions; the first one related to the 2011 guidance. If you could, just provide us with an idea of where do you see the biggest upside and downside risks to either revenue or margins guidance.

And the second question. You made a comment on the balance sheet and the financing of a potential, new, commercial program. I just wanted to -- If I understood correctly, you mean that, even a new program, you wouldn't need more equity to finance that program. Am I correct?

Those are the two questions.

A - Frederico Curado {BIO 2004589 <GO>}

Well, as far as downside to 2011 guidance, I don't see anything -- there's no major downside identified today -- nothing that -- we are already working to mitigate that risk. So, if there was --

FINAL

I will just call it to attention that we were conservative. And I kind of agree to that. But not conservative because we expect much better -- because we are expecting a tough environment. So I don't see much of a downside, other than we have to perform. As I mentioned, we have a few challenges for a few sales in the business jet area. But, we're talking about lower-value aircraft. So -- unit value aircraft -- We are fully committed and engaged to deliver that.

Upside? I think the fundamental upside would be exchange rate. If the exchange rate gets better, it's pure tailwinds. Do I think that's going to happen? No. I don't think so. As Cynthia mentioned, we are planning about BRL1.70. So we're actually below that. And we are committing to get whatever difference -- BRL1.67, BRL1.66, BRL1.68 -- we're going to do that anyway. We're going to find ways to compensate for that. But, if the exchange rate really is BRL1.75 or BRL1.80, that's going to help our numbers. Potentially, we'll get better numbers.

Today, as far as new program, it's too early to tell about raising equity. It is not -- Let's say it is not in our primary to-do list to raise new equity. If we launch a new program, we'll probably do that in steps -- you know, launch the concept. It's too early to really define how we're going to finance that. One of the sources will be, certainly, our cash flow generation. But that obviously would not be sufficient. We have a lot of room for indebtedness. So it's too early to tell.

I'm not sure if Cynthia wants to complement anything on that. Okay.

Q - Unidentified Participant

(inaudible) from Morgan Stanley. If there's any update on the potential order from the US Air Force for the Super Tucanos and, also, if there's anything going on with your China plant --

A - Frederico Curado {BIO 2004589 <GO>}

On the US, no. There's no news on that. Optimistically, I should mention to you that I was directly involved in the visit of President Obama to Brazil. And I was gratefully[ph] impressed by how well the Brazilian government received the US visit and how much closer the dialogue is now. So I really pray that this movement continues and Brazil and US gets closer because we have, really, the potential to together build an important -- a strong continent. We're talking about, between the two countries, over 0.5 billion people - - important markets, two large democracies, about the same age -- 500 years, each country, principles of the society, institutions. I think the US institutions are well developed. Brazil is probably the closest developing country to the United States as far as institutions than anybody else. And friendship between the two people.

So to provide products to the department -- Why I'm saying all that? Selling the Department of Defense in the United States is not an easy exercise. I think the more comfortable the two countries are, the more close they are, if they really engage and get more profound ties in the military, that improves our chances to participate. The airplane

is perfect to what they need; no question about it. Super Tucano is a very ideal aircraft. And it's ready today.

Competing aircraft -- first of all, they're not ready today. They need a few years for development and, most likely, will not be as perfectly adjusted to the RFP as ours.

But this is not the product only, of course. We have to take into account that geopolitical counts a great deal in those aspects.

China. Presidential visit next month. President Dilma Rousseff of Brazil will visit China. She will have a state visit. And, also, she'll participate in two major events. There is a BRIC conference or whatever arrangement they have. And, also, there is (inaudible), which is the equivalent of the world economic forum in Asia, both in the island of Hainan. So it's going to be a long visit.

Our expectation is that an outcome for our industrial presence in China is defined during that visit. So all the actions, all the discussions, they point towards a final outcome, hopefully positive, by the time of her visit, which is going to be mid-April, about a month from today.

Q - Unidentified Participant

The positive outcome that you are hoping for is to be able to produce E-jets at that facility?

A - Frederico Curado {BIO 2004589 <GO>}

Either that or the Legacy 650 there. It's less related to product. It's more related to our presence in China with an important industrial operation with the partnership with AVIC. This is institutionally and, let's say, at the company level, this is more important than to which specific product will be produced there. So either the 190 or the Legacy, which has, let's say, an interesting case as far as the tooling. It's actually more adaptable. The existing tooling is more adaptable to the Legacy -- it's a 145 derivative -- than the 190 actually. The investment is less, actually, to produce the Legacy aircraft. It's a promising market. And, as far as we are able to export 190s from Brazil to China, it's okay. I think our presence helps that case.

So, with that, one more time, we thank you very much for taking the time to be with us today. And I wish you all a great 2011. Thank you, very much. Have a nice day.

Operator

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

FINAL

Bloomberg Transcript

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.

Bloomberg Transcript