

## Q4 2017 Earnings Call

### Company Participants

- Eduardo S. Couto, Head-Investor Relations
- José Antônio de Almeida Filippo, Chief Financial Officer, Executive Vice President, Finance & Investor Relations
- Paulo Cesar de Souza e Silva, President & Chief Executive Officer

### Other Participants

- Cai von Rumohr, Analyst
- Joshua Milberg, Analyst
- Mariana Perez Mora, Analyst
- Noah Poponak, Analyst
- Peter John Skibitski, Analyst
- Ricardo J. Kleinbaum, Analyst
- Turan Quettawala, Analyst
- Victor Mizusaki, Analyst

## MANAGEMENT DISCUSSION SECTION

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

Okay. Good afternoon, everyone, and welcome to the Embraer Day 2018, Brazil. We'll start the conference call and we will review the Embraer's Fourth Quarter 2017 results. This conference call is being held during the Embraer Day with the presence of investors and market analysts. At this time, the conference will – the company will present its fourth quarter 2017 results and financial outlook for 2018. Afterwards, we will conduct a question-and-answer session and instructions to participate will be given at that time. As a reminder, this conference call is being recorded and webcasted at [ri.embraer.com.br](http://ri.embraer.com.br).

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

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

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 events and circumstances discussed on this conference call might not occur. The company actual results could differ substantially from those anticipated in the forward-looking statements.

Participants today on the conference call are Mr. Paulo Cesar de Souza e Silva, President and CEO; Mr. José Filippio, Chief Financial Officer and IRO; and myself, Eduardo Couto, Director of Investor Relations.

Now, I would like to turn the conference over to Filippio. Please go ahead, Filippio.

## **José Antônio de Almeida Filippio**

Okay. Thank you, Eduardo, and welcome everybody to our conference of financial results for 2017 and estimates for 2018. As usual, we're going to do the presentation and then we'll be ready for the Q&A. So, starting with the highlights of financial results 2017, we delivered 101 E-Jets, see page 4. Okay, we delivered 101 E-Jets and 109 Executive Jets delivering, reaching our delivery guidance. Net revenues in 2017 were \$5.8 billion, also in the guidance range.

Regarding EBIT, we reported adjusted EBIT of \$397 million with 6.8% margin. EBIT was \$50 million below guidance due to additional costs in our defense programs. We'll detail that later in the presentation. Adjusted EBITDA was \$713 million with 12.2% margin, below the guidance for the same reason already mentioned. In terms of free cash flow, we generated \$405 million, driven by working capital gains and lower investments. The total investments in 2017 were \$610 million.

Next page, for the highlights of the business units, start with Commercial Aviation, we delivered 101 E-Jets in 2017 and achieved a book-to-bill of 0.92, close to our 1 time (00:04:48) target. The E-Jet program reached an important milestone with the delivery number of 1,400 which was delivery of E175 to American Airlines. Our backlog reached 280 firm orders with a total of 715 commitments. We recently received the unique triple certification from ANAC, FAA and EASA for the E190-E2. In terms of delivery schedule, we confirmed the first E-Jet E2 deliveries for April 2018 to Widerøe from Norway. Continuing the E2 program, development in 2017 was successfully rolled out and had the first flight of the E195-E2 prototype. And finalizing the highlights of Commercial Aviation, the information that the E-Jets family reached the milestone for 1 billion passengers transported since entry into service.

So moving to next page, the highlights for Executive Jets, we delivered 109 Executive Jets in 2017, broken by 72 light jets and 32 large jets; including the delivery of the 1,100th Executive Jet in 2017. We also had the delivery of the first Legacy 500 assembled in Florida and the Phenom 300 was the most delivered light jet for the sixth consecutive year. In terms of product update, we launched the new Phenom 300E with new interior, increasing its competitive position. As far as customer satisfaction, we are ranked at number one in customer support for the second consecutive year by AIN.

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Next page, highlights of Defense & Security. Starting with the KC-390 Program, we achieved the initial certification with more than 1,600 hours of flight test. In terms of commercial activities, we delivered four Phenom 100 to the UK Ministry of Defense to be used as flight training. And also, we sold 18 Super Tucanos in this year and that aircraft was selected by the U.S. Air Force light attack experiment to do further demonstrations. In 2017, we successfully launched the Brazilian satellite in May. And finalizing the highlights of Defense & Security, we have the first flight of the new-generation Gripen.

Moving to next page, as far as corporate highlights in 2017, we launched the Passion for Excellence Program to gain efficiency and reduce costs. Also, we continue our compliance program improvement in 2017 for the first year of monitorship. And we had a new business - launched a new business which was dedicated to service and support. Regarding business innovation we operated (00:08:12) outposts in Silicon Valley and Boston and launched an international venture fund to explore possibilities in this area. Okay. With that, we close the highlights and we start the financial results.

Page 10, backlog, we reached the total of \$18.3 billion in the end of 2017, broken by 73% of Commercial, 23% Defense, and 4% Executive.

Next page. Net revenues, we had a total of \$5.8 billion in 2017, meeting the guidance. We had a reduction when compared to 2016, mainly due to the lower deliveries as already expected.

Next page. In terms of deliveries, starting on Commercial Aviation on the left, we delivered 101 E-Jets in 2017, within the guidance range. On the right side, Executive Jets, we delivered 109 Executive Jets being 72 light and 37 large, also within the guidance range.

Next page. Revenues by segment and geography. On the left side, revenues by segment, Commercial Aviation accounted for 58% of the revenues in 2017, Executive was 26% and Defense 16%. Regarding the breakdown by region, North America remains our major market; followed by Europe, Brazil and Asia with similar contributions.

Next page, revenue by business units and by quarter. Commercial Aviation reported a total of \$3.3 billion, within the guidance. Executive Jets was slightly below the guidance range as a consequence of an unfavorable delivery mix. Defense was slightly above the guidance range, reflecting weaker dollar against the real.

Next page, SG&A expenses. We reported a total of \$486 million of sales, general and administrative expenses in 2017, equivalent to 8% of the revenues from 9% in 2016. SG&A expenses were slightly above the previous year, primarily due to the weaker dollar against the real as those expenses are mainly in Brazilian local currency. Regarding selling expenses, we had a reduction when compared to the previous year, coming mainly from Executive Jets business.

Next page, as far as EBIT, the adjusted EBIT was \$397 million in 2017 with 6.8% margin. These numbers below estimates reflects the negative impact of \$50 million in the

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program development of the KC-390. Excluding that impact, the EBIT margin for 2017 would have been 7.7%, close to the lower end of the guidance as we previously indicated. Back to reported margin of 6.8% in 2017, the breakdown by business was Commercial Aviation 13.5%, Executive Jets breakeven and Defense negative 4.7%, actually the 4.7% negative would return on a positive 0.5% if you exclude that effect of the cost of the KC-390.

Next page, adjusted EBITDA, the total adjusted EBITDA for 2017 was \$713 million with 12.2% margin. The numbers were affected by the same (00:12:18) negative impact of the cost increase of KC-390 development program.

Next page, adjusted net income was \$280 million in 2017 with net margin of 4.8%. In terms of adjusted earnings per ADS and payout, the adjusted earnings per ADS was \$1.52 and the payout ratio was 26%.

In the next page regarding investments, we had a total of \$610 million of investments in 2017, broken by \$434 million in R&D and \$176 million in capital expenditures. In more detail, research was \$49 million, development was \$385 million, and capital expenditures was \$176 million. Most of these investments were related to the development of the E2 Program.

Next page, page 21, adjusted free cash flow. We've reported the free cash flow generation of \$105 million (sic) [\$405 million] in 2017 and \$407 million in the fourth quarter of 2017. This number was above our initial expectations and positively impacted by the improved working capital with an inventory reduction of approximately \$300 million, mostly, in Executive Jets, lower investments about \$50 million and sale of used aircraft owned by our leasing company.

Next page, capital expenditures. Our net debt as of the end of 2017 was \$4.2 billion and our cash position, \$3.89 billion, returning to a net debt of \$311 million, better than the previous year. Regarding our debt, its average terms was six years, very adapting and ready in terms of our product cycle.

Next page. Now we finished the financial results and we like to present our financial outlook. We usually do this in the beginning of the year. This information updates the preliminary guidance that was released together with the 2017 third quarter financial results in the end of October and don't differ much of those, but present more details.

So, on the next page, starting with net revenues and deliveries for 2018, we are estimating the total revenues for 2018 in the range from \$5.4 billion to \$5.9 billion. Revenues estimated by business units now including Services & Support business are \$1.35 billion to \$1.5 billion to Executive Jets, \$0.8 billion to \$0.9 billion to Defense & Security and \$0.9 billion to \$1 billion for Service and Support. In terms of deliveries, for Commercial Aviation, the range between 85 deliveries and 95 deliveries and for Executive Jets, 105 to 125, broken by 70 light jets to 80 light jets and 35 large jets to 45 large jets.

Next page, for results on cash, we expect EBIT to be in the range of \$270 million to \$355 million with margin range from 5% to 6%. EBITDA on the range of \$540 million to \$650 million with the margins between 10% and 11%. Free cash flow is expected to be a consumption of \$100 million or better. And investments are expected to be \$550 million, broken by \$50 million for research, \$300 million for development and \$200 million for capital expenditures.

Next page. We consolidate and present our 2018 outlook. So, with that, we conclude the presentation and we now move into the Q&A session. Thank you.

## Q&A

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

Okay. Thank you, Filippo. Now we're going to start the Q&A section. but first we'll start with the audience here. If you have a question just raise your hand, we have mics on the room. We'll start the questions from the audience. Thank you.

[Foreign Language] (17:37-17:44) Should I do it in English or in Portuguese? Sorry. Sorry.

English will do.

My question was the deliveries in 2019 – or actually not just 2019, but beyond 2018, for which should be a lower deliveries year as per the guidance provided by the company. My question is actually how best should we expect these deliveries to return to regular levels or closer to 100 units on the Commercial division? Thank you very much.

### A - José Antônio de Almeida Filippo

Thank you for the question. I think we already indicated that before when we said that there is going to be a transition period between the phase in and phase out of E1 to E2. So, we still expect 2018 and 2019 to be weaker years in terms of deliveries, but we expect in mid-term this would recover. That's typical when we have two models at the same time. It brings some inefficiency. Also, the learning curve of a new model takes a little bit longer than a matured one. So, we expect to be in mid-terms something better, maybe two, three years, that's what we said we'll be recovering to normal levels. Normal levels will mean historical couple of years.

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

We'll take another one from the audience. Turan?

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

Turan Quettawala from Scotiabank. My question was on your 2018 margin guidance. If you look at the margin – when you guided for 2018, back in October, you had provided the same guidance of about 5% to 6% EBIT margin, but at that point, you were expecting a higher margin in 2017. So, your margin in 2017 is about 100 basis points lower than what

you were expecting it to be in - back in October. So, my question is how comfortable are you with that 5% to 6% EBIT margin guidance for 2018 and why is - is there any risk to that and what are you doing to make sure that whatever pricing, I guess that's been maybe a bit more negative, is that coming back to give you confidence on that 2018 margin target? Thank you.

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

Okay. Thank you, Quettawala. I'd say that what happened 2017 was this cost recognition that we have to make at the end of the year in the KC-390 program. If we add that back, we're going to go to the 7.7% margin in 2017, which would be very close to the lower end of the guidance, which I already indicated that time that we expected to have. And by the way, it's good to recall now that this \$50 million, it was not something that was already cashed out. This is a recognition of the problem, this has to be achieved or incurred going forward. It's already included in the calculation for the future 2018. So, we still maintain it as 5% to 6%. So, we think that excluding that effect, we will basically where we expect it to be in 2017. So, we're still maintaining that for 2018. That's what we expect.

By the way, let me add an information to you. In terms of how we build up the 5% to 6%, normally we give some information on this. In terms of Commercial Aviation, you think about something about high single-digit. In terms of Executive Jets, low single-digit. For Defense & Security, low single-digit as well and Services & Support, low double-digit. That combination will lead us to the 5% to 6%. We don't send out guidance specific for margins to the business.

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

Thank you.

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

Okay. Now, we're going to take a question from the phone. Operator, I think we have Pete Skibitski from Drexel Hamilton. Can you open his line, please.

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

Good morning. Can you hear me?

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

Yes.

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

Yes, we can, Pete.

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

Okay. Great. Paul, good morning. Is there anything you can add to the same in the release regarding a potential tie-up with Boeing in terms of maybe how it might be structured, and if you think the Brazilian government would approve such a deal?

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

Hi, Pete. Hello, everybody. Good afternoon. Well, we continue to work with the government, so there is a working group that was appointed by the government. So, we are engaged with them in order to find a structure that can work for all the stakeholders. So, we have of course our shareholders, we have the government, we have the buyer, we have Embraer. So, we have to make sure that we have a structure that can be acceptable by the parties, so that's what we are doing now. And there is a very good engagement, so that's all I can say, so I can't say more than that.

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

Okay. Understood, understood. And if I could, I'd like to ask a follow-up on the KC-390, I am wondering when you expect to firm up the order from SkyTech for the LOI for six KC-390s and when first delivery might be?

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

Well, we are working on that. So, this LOI was announced if I'm not mistaken, the Singapore Airshow, so it's a good sign. So, we are very optimistic that we can sign and engage in a firm contract as well this year. So, it's a good addition to - it would be a very good addition for our KC-390 program, and hopefully so, we can move forward with that until end of this year.

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

Okay. Thanks very much, guys.

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

Thank you.

**Operator**

Okay. We're going to take another question from the phone. The next question will come from Cai from Cowen. Cai, the line is open. You can ask the question.

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

Yes. Thank you very much, guys. So, your Executive Jet book-to-bill looked particularly low in the fourth quarter. Can you comment on that and give us color on demand of the Executive Jet sector?

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

Yes. So, thanks for the question. So, the Business Jets business, so, is improving gradually, right? So, I think until last year, we saw very challenging markets. If not mistaken, the industry all together delivered last year 641 units in 2017; 2016 was just one unit right below that, 640. So, the numbers are (00:25:18) still last year was under huge pressure. However, we are seeing signs of smooth recovery, if not an aggressive one. But however, so good signs on the used inventory. So, the prices are not falling any further. The used

aircraft prices, and the market is beginning (00:25:46) to clear on the older jets - used jets. So, that's a very positive sign because the next step now definitely will be about people and companies looking to buy new jets, brand new jets. So, the tax reform by Trump in the United States is a big driver for the Business Jet business. Together with that, the growing GDP in the United States going forward will be also a big driver, so don't forget that 60% of the Business Jet market is within the United States. So, we are more bullish this year that the Business Jet unit will have more opportunities.

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

Thank you very much.

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

Okay. Now, we're going to get back to the audience. So, if you have a question, please, on the left.

**Q - Ricardo J. Kleinbaum**

Hello. My name is Ricardo from BNP Paribas. I would like to ask a question about the KC program, when the plane is in line production, do you expect the gross margin to be similar as the Commercial Aviation or not?

**A - José Antônio de Almeida Filippo**

Yes, we have this - we're starting up the process of manufacturing now, first delivery will be in the second half of this year, and of course, it depends on the type of order, because this product the type of customer is not typical like the Commercial area, so each plane tends to be more customized or so it includes other (00:27:49) than itself. However, we believe that they can be in the level of the Commercial that you mentioned, so something like a two-digit, something between mid-single - mid two-digit margin would be reasonable to see (00:28:05) on top of margin.

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

Anyone else from the audience? On the right?

**Q - Mariana Perez Mora** {BIO 16856823 <GO>}

Mariana Pérez Mora from Bank of America Merrill Lynch. Could you please drive us through the puts and takes on the free cash flow from the positive \$400 million free cash flow this year to a negative \$100 million next year?

**A - José Antônio de Almeida Filippo**

Yes. I think we had - Mariana, thanks for the question. We had a situation in 2017, which were first like I mentioned the adjustment in the working capital, we saw a reduction in inventory especially in finished goods. And the management, the way we manage the production vis-à-vis the delivery, so we end up with lower inventory in the end of 2017, so that is something that we should not expect going forward so the adjustment, part of



focus on the margins and the price rather than deliveries itself, I think was a major impact for 2017 that we don't expect to see the same magnitude through 2018.

Another thing was the reduction or the lower investment that we have, \$50 million, we guided \$650 million and we end up \$610 million or \$40 million. That also have, we're thinking of the \$550 million for 2018, we think we're comfortable with that and then the opportunity of selling some used aircraft that we have in 2017. We had a \$1 million opportunity on some used markets, especially in Africa, smaller aircraft, that we took that opportunity. So, it's more like a one-time thing that we don't count on that to happen again. So, that's basically how we bridge or what drove us to the improvement in 2017, 2018; of course, there is a commitment for us to be disciplined in terms of generating cash and to take those opportunities again. So, as we can, definitely we're going to be looking for opportunities to improve the cash generation, but at this point, our best expectation for 2018 would be the negative \$100 million, which we think is a little bit better than what we initially expected for 2017.

**Q - Mariana Perez Mora** {BIO 16856823 <GO>}

Thank you.

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

Thank you. Thank you very much. (00:30:28) with Morgan Stanley. Just a follow-up on this question, actually a clarification. On the - one of the reasons for the lower free cash flow generation, I think you mentioned, the lower investments. So just to clarify, if I remember correctly, we're talking about something like \$430 million, around \$430 million in terms of R&D over the past two years, and I thought that that number was coming down in a major way to \$350 million or so next year. So just a clarification on that point, if - when you mentioned that investments were a little bit lower than last year. Thank you very much.

**A - José Antônio de Almeida Filippo**

Okay. Thanks, (00:31:12). I will say that, of course, we are still in the process of developing the E2, which was our major program that still, as you know, entering to service of E190 will be next this year, in April, the first delivery, E195 next year and the E175 we rescheduled that for 2021. So that bring us still to the development phase of this program. Of course, as we get to this point of go-ahead today, we start to think about starting to decrease, but not the major decrease.

So, I think that the extension of the E175 already brings us to more of investment in a couple of years, but we don't see that in 2018 will be that (00:31:59) I understand that you're referring to in normal levels, like if you take out some major investment in a new product or in a product, (00:32:11) the level that we have a level of depreciation, assuming that we're going to be reinvesting depreciation, talking about level of 300, 350, that's basically, I think what we probably have in reference that we mentioned sometime before.

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

Okay. Let's take another one from the phone. Next question will come from Noah Poponak, Goldman Sachs. Noah, your line is open.

**Q - Noah Poponak** {BIO 16071528 <GO>}

Hi, everyone.

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

Hi, Noah.

**A - José Antônio de Almeida Filippo**

Hi, Noah.

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

Hi, Noah.

**Q - Noah Poponak** {BIO 16071528 <GO>}

I wanted to ask – if you looked at the last few years on average, what has been the average, rough order of magnitude change in pricing annually across the business, I know it's different by segment, but if you could give us any indication of that? And then, separately, what has labor cost inflation been on average over the last few years? And then, what are you expecting for those two items going forward?

**A - José Antônio de Almeida Filippo**

Noah, in terms of price, we saw – of course, remember that we had the larger campaigns in the U.S., we are delivering most of the Phenom these days that's why we already showed that our delivery piece is larger in the North American market. Those campaigns as we have larger amount, there were price pressures, and we already indicated that. However, because of that, we were able to reduce cost as well.

The standard type of plane helped us to do this. Our focus on cost reduction already got some good results. So, price was reducing. I don't say that this is dramatic reduction. It depends of course like you said in the size of the campaign, the size of the order, on the conditions itself, on the competitive situation. But I think that price reduction was not major, but it was followed by the improvement in efficiency in terms of keeping the margins, if you follow that that's what we said. This is more commercial, but again, it depends more on the specific campaign in the deal.

In terms of Executive Jets, we don't see a major reduction now. And by the way, as you know, we have been focusing on the quality of the sale, so not bringing necessarily the volumes, but getting price and we still saw this year, the first quarters of year already indicated that and now we're confirming that the price was a little bit above the average that we had before. So, of course, we should not deliver the same number of aircraft on that – it's a little bit less, but keeping a certain level, we don't see that major reduction. What's the second question, Noah?

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

In terms of labor cost?

## A - José Antônio de Almeida Filippo

Labor cost.

## Q - Noah Poponak {BIO 16071528 <GO>}

Yeah.

## A - José Antônio de Almeida Filippo

Labor cost, as you know inflation in Brazil has been low and labor cost tend to follow that. We had in 2015-2016 something around 5% - 5% to 6%. Last year, 2017 was 2%, labor adjustment in average to give you an idea on that. And we still see inflation under control in Brazil, we're not increasing. So, we tend to see the labor cost should follow inflation rate, which is very low at this point. So, we don't expect that to be a major concern going forward.

## Q - Noah Poponak {BIO 16071528 <GO>}

Great. And then, if I could ask one more, in some of your more recent communications with the market, your New York City event and some others that I thought you sounded fairly bullish on the degree of regional jet campaigns and the potential for new orders there. Obviously, I'm looking at on a relatively small sample size of time, but there hasn't been anything announced since then. Maybe just update us on that. Are you still seeing as many opportunities? Have some of them come and gone or any explanation you can give as to why they're being stretched out if they are even being stretched out?

## A - José Antônio de Almeida Filippo

Thank you. And so, I think last year we had almost a 1:1 book-to-bill, was a relatively good year, right? So, when you look to the other guys, so I believe we were the best in terms of taking new orders, that was very positive. Going forward now, so - and John will talk more about that when he'll make his presentation, but with the certification of the 192, which occurred this month and the first delivery next month in April, of course, the dynamic will be different. So, we have an aircraft that is delivering more than we had promised when we launched this product. Fuel burn is much better, range is better. So, the performance of the growth of the aircraft overall is peaking such that the markets will appreciate as it enters into service. Having said that, we are engaged in many campaigns, not only in the United States, which is our largest market now if you see the last year, but very good campaigns all over. So, we are quite bullish going forward.

## Q - Noah Poponak {BIO 16071528 <GO>}

Okay. Great. Thank you.

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

Okay. Next question from the audience here.

Talking about Defense & Security, what do you expect for growth opportunities in other revenues like radars, satellites, maintenance like OGMA and what about the expectations

for margins in these other revenues?

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

Well, overall speaking, I think the Defense business is - has a very good future. When we look at the KC-390 - the opportunities that we may have in the whole world, so it's going to be great. So, we are on time with the development for the first delivery is going to be this year. In Defense, you have to deliver the aircraft to your air force in order to have a market recognition that you have gotten there, right? So the KC-390, is a very complex aircraft and I'm sure that as we start delivering to the Brazilian Air Force this year, the interest will be even greater. So, there are 2,700 C-130s in operation, 34 years old in average. So, it's a huge potential for the KC-390. So, I'm not saying that we will get all these replacements, but if we got a portion of that, let's say one-third of that, right? So, it's going to be great. It's going to be really something that will boost a lot the Defense business and we have this opportunity to grab the sales going forward.

So, the interest in the aircraft is absolutely fantastic. So, we are seeing a lot of governments like countries more and more interested in seeing this aircraft. These recent LOIs for SkyTech, I think was the, I'm sure that is a tremendous opportunity to showcase also the KC-390 to other countries, since this SkyTech is not a leasing company but they're an operator of this type of aircraft for its special missions, right?

So, it's going to be very important. So the Super Tucano is an amazing aircraft. So, it's tested, it's in operation, is doing absolutely fantastic for the countries that have bought it. So, look at the United States Air Force, they have bought for the Afghanistan operation, and they are very much involved in other projects. And one that of course everybody is looking for in special years is for the replacement of the A-10 in the United States. There are opportunities here for maybe 300 aircraft. And the U.S. Air Force like the Super Tucano a lot. So, I'm not saying that we will win, but we have definitely a great opportunity to make this happen. So, we are quite bullish on that.

On the other areas that you mentioned, I think we have to be very realistic here, right. So, the other areas are more linked to the Brazilian budget (00:42:03). So, we have to see this in a way that we don't expect that there will be a big boost we're going to see, so we need the budget, we need the budget from the government in order to enter into these new products.

Having said that, I think there are some priorities that the government will have to make. Like for instance, the second satellite, SGDC, since the first one was launched this year and there is a huge need for this kind of right investment, right? So, because Brazil does need additional Internet band, right, for the - so I believe this will come. So, let's hope that this year, until the end of this year, so the Brazilian government will take a decision there.

So regardless the new president, so this is an area that Brazil will have to invest. And the Sisfron project will continue maybe not in the same speed that we would like, but likely to come, and for OGMA, I believe OGMA is set for growth because it's - we are investing in OGMA, so we are giving OGMA the opportunity to have more business. So, we are integrating OGMA more into the other business units. So, OGMA is set for growth, so it's

already like a profitable business, but now, we have to grow. So, we are very optimistic overall speaking in the sense that we (00:43:59) start to hear because of the light jets, we will not have other thoughts to present to you. Okay?

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

Okay. On the right side, a question from the audience.

**Q - Joshua Milberg**

Good afternoon, everyone. Josh Milberg from Morgan Stanley. I just wanted to go back quickly to the question of pricing. I think that you would suggest that in the recent past that perhaps one source of pressure there, not just on pricing but also on profitability in 2018, could be that there's a special configuration of your E175 aircraft and I was just hoping you could kind of update us on what the situation is with that configuration. If you've already started delivering that aircraft and maybe what the magnitude of the impact could be in terms of margins?

**A - José Antônio de Almeida Filippa**

Well, there are big opportunities in the - right in the U.S., from 50 to - up to 106, right? So, depends on the airlines, so they can go not exactly to the 76 seats, but they can go up to 70 seats. So, offering the 76-seater in a configuration that has less seats, is a good opportunity for the airlines to upgrade from 50 seats, right, or replace the old CRJ700 or E-Jet 170, right? So more brand-new aircraft. So, we believe that these trends may continue. Of course, it depends also whether or not there would be more scope of relief for the airlines to go straight to the 76 seats. But we see, as of today we see a very good opportunity to increase the number of the E175 in the United States, so a big opportunity. Did I answer your question?

**Q - Joshua Milberg**

Yeah. I think so, maybe if you could just touch on the question of pricing because our understanding had been that the 70-seater configuration does have a lower selling price and that in turn might explain some of the downsides to profitability in 2018. And I was also just wondering if that had been a variable and that's behind your margin performance in the fourth quarter itself already.

**A - José Antônio de Almeida Filippa**

No, no, not at all. And for 2018, so our margins in Commercial Aviation will be a little bit lower, why? Because we are in a transition period, right? So, we are moving from E1 to E2 gradually, right? And we have the ramp-up cost, so we have the introduction cost of the - right, of the E2. But as far as the E175 is concerned, so margins are good.

**Q - Joshua Milberg**

Okay. I just understand that in addition to the ramp-up of the E2 that this configuration could also be a variable and - but you're saying that, that it's is not, it's not (00:47:38)

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## A - José Antônio de Almeida Filippo

It's not, yeah.

## Q - Joshua Milberg

Okay. Thank you.

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

Okay. Another one on the left side.

Hello, guys. This is Lucas (00:47:49) from (00:47:50). A more broad question on my side. Have you guys perceived any change in the commercial behavior of Bombardier after the deal was (00:48:00) and is this positively affecting commercial aircraft prices already?

## A - José Antônio de Almeida Filippo

Well, the announcement by Airbus and Bombardier that moment was very important, right? Because first of all, it validated the segments between 100 and 156, right? So, it definitely was a big validation by Airbus that it's an important segment and that Airbus should be there, right? So, this of course is bringing more interest from the market, in general, that's why I mentioned before here that we are seeing more activity, we are engaged in very good conversations globally.

We can't see yet any change because Airbus cannot work with Bombardier now, so, they have to wait until all the authorities in many countries clear the deal, right? So, they are anti-trust authority. So, I think so far only Germany has cleared, so it's still missing many others and of course other steps as well going forward. So, I believe only in the third - in the third quarter or so this year that the Airbus and Bombardier will do a joint to joint efforts, right? So, so far this is as usual, more interest from the markets, the E195-E2, especially the E195-E2 has been perceived a very efficient aircraft, and so, we are very bullish on the segment. And John will elaborate more on that.

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

Okay. Now we'll take our final question from the phone. The final question comes from Victor Mizusaki, Bradesco. Victor, your line is open.

## Q - Victor Mizusaki {BIO 4087162 <GO>}

Thank you. I have two questions here. The first one is a follow-up on the sales campaign, can we assume that the negotiation with Boeing will likely delay any big announcement in the short-term? And the second question with regard to your - the impairment of \$54 million in Executive Aviation. I don't know if you can you give any color on this and what would be your operating margin in Executive Aviation in Q4, if we exclude this impairment?

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

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Okay. For your first question, no it's not – we can't say it. So, it's a – we don't know, right? So, we don't know. So, we are – I think what's important is that all the parties are working very hard to have an outcome, right? An outcome as soon as possible. So, all the parties involved, so they understand the need to have an outcome as fast as possible.

From our side here, we don't want to go too long on that. We do recognize that a solution for that or an outcome, so because we don't know if it's going to – if it's going to be happening or not. So, it's not possible to like say this at this stage, but we are working hard to have as I said an outcome very soon.

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

And Victor regarding the margin on Executive that you asked, we – this margin would breakeven that we set for 2017, was already not impacted by the impairment. For 2018, like we said, we expect in the low single-digit for the Executive Jets and we have to take into account that we are not considering the service revenues on the Executives for 2018.

Now, we separate that, so only the Executive itself is low-single that we expect for 2018. So, there is still work being done. As you know, we have a new leadership in Executive Jets since the first quarter of 2017. So, adjustments are being made. And I already pointed out about the reduction in selling expenses, which is not prioritizing what to do, focusing more on how you spend in terms of commercial – sorry, selling expenses and marketing activities. So, we believe that's going to be an improvement if we compare that also with the past, and adding that, we expect the market to start to be better going forward, that's basically the points for the margin.

### **Q - Victor Mizusaki {BIO 4087162 <GO>}**

Okay. But Filippo, and specifically about the impairment, this is something related to the intangible of, I mean, Executive Aviation, or let's say it is a write-off of inventory?

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

No, that was related to assets associated to the Legacy 650 that in terms of how we see the projection of sales and manufacturing of that aircraft. We had to do the calculations and we returned to a negative net present value, so we had to write off this as an impairment, this is the same as the write-off of the assets associated to the specific program, that's what happened.

### **Q - Victor Mizusaki {BIO 4087162 <GO>}**

Okay, thank you.

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

Okay, I think that concludes our fourth quarter 2017 earnings call. I want to thank you all over the phone. For those in the audience, we're going to follow with the individual presentations after a short break. Filippo, do you have any comment?

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[Abrupt End]

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