Y 2018 Earnings Call

Company Participants

- Paulo Sergio Kakinoff, President and Chief Executive Officer
- Richard Freeman Lark, Chief Financial Officer

Other Participants

- Dan McKenzie, Analyst
- Duane Pfennigwerth, Analyst
- Michael Linenberg, Analyst
- Pedro Bruno, Analyst
- Petr Grishchenko, Analyst
- Roberto Otero, Analyst
- Rogerio Araujo, Analyst
- Savi Syth, Analyst
- Unidentified Participant

Presentation

Operator

Welcome to the GOL Airlines Fourth Quarter 2018 Results Conference Call. This call is being recorded and all participants will be in a listen-only mode during the company's presentation. After GOL's remarks, there will be a question-and-answer session. (Operator Instructions) This event is also being broadcast live via webcast and may be accessed through the GOL website at www.voegol.com.br/ir and the MZiQ platform at www.mziq.com. Those following the presentation via the webcast may post their questions on the platform and their questions will be either answered by the management during this call or by the GOL Investor Relations team after the conference is finished.

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

At this time, I would like to hand the call over to Mr. Paulo Kakinoff, please begin.

Paulo Sergio Kakinoff {BIO 5160310 <GO>}

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

Richard Freeman Lark {BIO 3484643 <GO>}

Good morning. Good to be with you today.

Paulo Sergio Kakinoff {BIO 5160310 <GO>}

This morning, we released our fourth quarter figures. Also we made available on GOL's Investors Relations website three videos with our results presentation, financial review and brief Q&A. Once again, we improved operating indicators. In the quarter, GOL's RPKs increased by 3.5% from BRL9.9 billion in fourth quarter 2017 to BRL10.2 billion this quarter, driven by a 3.4% increase in the number of transported passengers. Strong demand allowed GOL to continually driving yield through dynamic revenue management. Average yield per passenger increased by 6.6% quarter-over-quarter, reaching BRL0.29. Supply growth ASK increased 2.4%, compared to fourth quarter 2017, driven by a 1.9% increase in seats, partially offset by 2.3% decrease in take off.

The average load factor was 81.9%, an increase of 0.9 percentage point compared to same period in 2017. For full-year 2018, RPKs increased by 3.2% primarily due to a 2.9% increase in the number of transported passengers, with yield growing by 7.7%. ASK's increased by 2.9%, load factor was 80%, 0.3 percentage point increase compared to 2017. We continued to drive strong revenue growth, the combination of higher demand and optimized pricing resulted in net revenue for the quarter of BRL3.2 billion, an increase of 10.1%, compared to the fourth quarter 2017. Net RASK was BRL0.256 in this quarter, an increase of 7.5% over same period 2017. Net RASK increased 7.7% quarter-over-quarter, reaching BRL0.239. Average fares increased by 6.7% from BRL330 to BRL334.

For full-year 2018, net revenue was BRL11.4 billion, 11% higher than the prior year. GOL's 2019 guidance is for net revenues of approximately BRL12.9 billion. GOL's current network serves higher yield routes and is the leader in the domestic market. We see market share of 36%. GOL is also a leader in the corporates customer segment, we have the largest market share of business traffic in Brazil. By the end of 2018, six 737 MAX 8 aircraft had already been incorporated into our fleet, providing us with lower operating expenses and expanding our network, allowing us to serve new destinations in South America, the Caribbean and United States.

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

Richard Freeman Lark {BIO 3484643 <GO>}

Thanks, Kaki. First, we would like to comment about our controlled cost environment. Total CASK in the fourth quarter was BRL0.2022, 2% lower than in the same period of 2017. On an ex-fuel basis, CASK fell by 19.4%. Our CASK ex-fuel and ex-aircraft sale and costs from maintenance of aircraft due to the execution of the fleet renewal plan were BRL0.1445, 3.9% higher than in 4Q '17. GOL remains the cost leader in South America for the 18th consecutive year.

Thus our margins remain solid, while the average price of jet fuel increased by 15.6% in this quarter over the third quarter of '18, the combination of stronger pricing, higher demand and the execution of our fleet renewal plan permitted GOL's operating income to reach BRL672 million and the EBIT margin to reach 21% in the fourth quarter of 2018, which is the highest EBITDA margin since 2006. EBITDA was BRL851 million in this quarter and EBITDA margin was 26.6%. EBITDAR was BRL1.2 billion, representing a 36.3% margin.

For the full-year 2018, EBIT margin was 12.3%, a growth of 2.7 percentage points compared to the full-year 2017 and operating income reached BRL1.4 billion. GOL's 2019 guidance is for an EBIT margin of approximately 18%. Second, we want to highlight our cash flow management, a combination of operating cash flow generation of BRL803 million in the quarter and stable cash liquidity improved the company's financial flexibility, total liquidity including cash, financial investments, restricted cash and accounts receivable was BRL3 billion at the end of 4Q '18.

Third, we'd like to share the continued success of our liability management program, our net debt excluding perpetual bonds, the last 12 months EBITDA ratio was 2.1 times at December 2018, improving versus the year ago metrics of three times. We finalized a series of deleveraging initiatives throughout the year. We repurchased our bonds with maturities in 2018, 2020, 2021, 2023 and 2028. In October, GOL successfully concluded a liability management and refinancing exercise on the debentures issued by its wholly-owned subsidiary GOL Linhas Aereas or GLA. The total amount of BRL1.025 billion was fully amortized in a new series of non-convertible and unsecured debentures of BRL888 million was issued, resulting in a reduction of net indebtedness of BRL138 million. GOL also amortized other short-term debt using funds from the generation of operating cash flow.

These transactions represented additional deleveraging of GOL's balance sheet and better match GLA's operating cash flow generation with the amortization of its liabilities. Our liability management activities have reduced the company's cost of debt and improved it's credit metrics. Today, the average interest rate is 7.7% for local currency debt and for dollar-denominated debt the average interest rate is 6.8%. GOL has maintained its commitment to financial discipline, managing the effects of Brazilian currency through our efficient capacity management and dynamic yield management. For 2019, we expect our domestic capacity growth to be between 2% and 4% and our international capacity growth to be between 35% and 45%. Non-fuel CASK is expected to be around BRL0.13. We have projected EBITDA and EBIT margins in 2019 based on IFRS16 at around 28% and 18% respectively. Leverage measured as net debt excluding perpetual debt over EBITDA for 2019 should be 2.9 times, reflecting our commitment to reduce leverage in our balance sheet.

Now I would like to return back to Kakinoff.

Paulo Sergio Kakinoff {BIO 5160310 <GO>}

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

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

Questions And Answers

Operator

Thank you. (Operator Instructions) The first question today comes from Duane Pfennigwerth with Evercore. Please go ahead.

Q - Duane Pfennigwerth {BIO 7329167 <GO>}

Hey, thank you. So, just with respect to the domestic capacity outlook, which remains disciplined, can you talk about flexibility that you have to ramp that up if in fact a big chunk of domestic capacity goes away or if there is a void in the market, question one. And question two, have you been approached by lessors to take over any aircraft, it maybe a different type in that eventuality?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Good morning. Thank you very much for the question. Actually, you probably will never laterally implement the restructuring plan by the end of 2015, 2016. We have renegotiated our leasing contracts in order to create the kind of flexibility that we could use in situations like this. At the moment, the company is fully prepared to either grow or to reduce its current capacity by 4 percentage points in a very short-term. So we do not believe that it's going to be needed at least of course during the current scenario, the current landscape. But we are fully prepared to fast react without changing our -- sorry without jeopardizing our main dealer, which is the incentive with structure. So we can't get access to even more planes than the 17 77 MAX that we are supposed to receive this year and include also -- postpone some of the current leasing contracts in order to increase the number of aircraft serving in our fleet. So we reached a greater than higher demand than the post year also that we have already shared with you. And if it's come, it is going to come and we will be fully prepared to observe it. Even if we have one of our competitors mean given us a further opportunity to increase our on-demand, I think that we are capable of getting it to without any major movements from our side.

Q - Duane Pfennigwerth {BIO 7329167 <GO>}

Thanks. And then just for my follow-up, you've given the forward load factor here into January is on the boards and February up one, I wonder if you could comment on yield trends beyond the load factor for January and February? Thanks for taking the questions.

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

Yeah, sure Duane, for February, which you know one-off traffic starts next week, but we're seeing around about a 15% increase in sales, in other words receivables, in other words you know paid tickets of which around a third of that is volume, about a 10% that is price year-over-year comparison about a 5% increase in volume and 10% increase in fares which kind of pull us into around a 15% run rate increase of sales. If you take that on a dollar basis, year-over-year remembering that we have an increased capacity is virtually the same as it was last year. It's almost BRL100 million in additional run rate of revenues on top of that, that's kind of like the February trend. For year-to-date similar trends with around a 15% increase in sales, January had a higher portion on the volume side then on the fare side, but year-to-date the run rate of sales for January and February about BRL200 million above what they were in the previous year end, you know, keeping in mind that capacity is still, growing in very low-single digits, you know everything I'm saying is domestic market.

Q - Duane Pfennigwerth {BIO 7329167 <GO>}

Okay, thank you.

Operator

The next question comes from Michael Linenberg with Deutsche Bank. Please go ahead.

Q - Michael Linenberg {BIO 1504009 <GO>}

Yeah, hey. Good morning, everybody. Rich, as we think about 2019, this year you had a healthy amount of gains or you had aircraft sales, you also had some of the re-delivery costs associated with the aircraft and engines. As we think about 2019, what is baked into your forecast as it relates to future aircraft sale gains and/or incremental costs associated with returning aircraft back to the lessors. In other words, you're, -- when we think about '19 your fleet transition program, how much of that is going to have an impact on your P&L, maybe similar to '18 or is it, is it going to be a bigger impact rough numbers would be helpful. Thank you.

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

Sure, sure. Yeah, the short answer is, in terms of our guidance, there's is a neutral or zero effect in there of the net effect of any potential gains on aircraft sales, less the cost of the return of those aircraft, zero in those numbers. '18 was extraordinary, because we took advantage last year of some very particular phenomena that happened in our markets, which was a temporary increase in availability of Max aircraft.

You remember we announced those direct operating leases in October, 11 Max is to come in the second half of this year or in the first half of next year. And that allowed us to be more aggressive on the disposition of aircraft in our NG portfolio, for which we continue to have good demand. And you saw the transaction in the fourth quarter which we monetized 13 with a net effect of that was basically just to accelerate our transition from the NGs to the Max.

Now generally we are budgeting from a operating perspective, the continued disposition of one to two NGs per quarter. So it is possible that this year based on market conditions, if market conditions continue we will dispose of some additional NGs this year. But we're not budgeting anything in there or it's not in the guidance. But we may continue to take advantage of the high demand for these midlife NGs, which we've seen from the market. Our ability to do that or accelerate that is contingent upon our ability to get Max's to replace those aircraft in the fleet. And so that's how I would guide you on that.

Q - Michael Linenberg {BIO 1504009 <GO>}

Okay, great. And then just back to your comments on February and the strength there. How much of that is really organic or are you actually seeing some share shift from one of your competitors are you picking up whether it's volumes are getting better prices, sort of that's the A part of the question. The B part of the question is, what -- how does the competitive capacity look out over the next couple of months, maybe quarter or so vis-a-vis Avianca Brazil, what are you -- what are you seeing in the markets right now?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Yeah, definitely we have kind of systems traffic shift.

Q - Michael Linenberg {BIO 1504009 <GO>}

Okay.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

But is not possible to preside how much are they. I would say that most of the growth comes from the organic, additional demand that they are getting from the market. I wouldn't say that we had it because, if you see their competitive deterioration is so far quiet marginal, I mean losing one to two percentage points and then given as an additional demand. I believe that certainly that market will continue to react rationally, even facing a further disruption in the market. But we also believe that Gol itself has played a major role in showing to the market a pre-disciplined capacity, pre-disciplined offer and I think that the market has no reason to change this dynamic anytime soon, even if you're going to have any kind of unexpected disruption coming from the competitor. So, I am pretty optimistic in that sense.

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

Yes, historically remember, domestic Brazil air travel has grown at about two to three times GDP. So this year, they expect -- the expectation of GDP growth here according to Central Bank is around 2.5% and that consistent with also the ABEAR, which is the Airline

Association here Brazil are expecting demand, domestic demand in the range of 5% to 7%. And so that's really what's driving the profitability here, supporting both yield, as well as just the overall volume increase. And this is been bouncing up and down for about I would -- since the fourth quarter of 2017, there has been this uplift. There was a suppression last year with the trucking strike in the middle of the year which basically collapsed the demand curve for about four months to five months. And then we had the elections, but pretty much since the elections were over and the certainty on that was installed. This is a phenomenon we've been -- I said, I think in the longer sense it's been since October of '17 pretty solid. But since November of '18, it's been even more solid. And it should also -- Carnival is in March this year, it was in February of last year. And so that was a positive for extending the summer travel season here in Brazil an additional month. So the year-over-year comparisons for the Q1 will also be helped by the fact that, we gain in the month of February onto the high season for 2019.

Q - Michael Linenberg {BIO 1504009 <GO>}

Okay, that's great. Can I just -- just one other quick, just squeeze in one here on your new services to the US. The only thing I wanted to comment, I thought it was interesting in your press release, you sort of highlighted the fact that you are the only airline that offers flights from Congonhas to the US, you listed other markets, but the US among international markets which presumably you're marketing these flights as one stops over Brasilia and Fortaleza. And I'm just curious if you are actually carrying decent loads that originate in Sao Paulo, that make their way up to Orlando and Miami.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Yeah, I can tell you without giving any further strategic disclosure that have two digits load factor being raised here in Congonhas to travel to Miami and Orlando mainly via Brasilia. So we have less than one hour connecting time in Brasilia, which makes this product pretty attractive to the travelers leaving in the neighborhood of Congonhas airport which means the highest portion of the local market. You can spare easily one hour avoiding the traffic within Congonhas and Guarulhos, having a quite pleasant experience connecting in such efficient airport as Brazil. So we had a considerable portion of our load factor in those flights being -- being raised here in Congonhas.

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

Yeah, we as Kaki said the taxiing time from Downtown Sao Paulo to Guarulhos is longer than the turnaround time and connection time in Brasilia. We've -- goal is over a period of several years built up significant presence in Brasilia and we -- so we have a lot of connectivity there. I took a flight to Miami on Sunday, you get on the plane here at around seven in the morning and you're in Miami at about 3:30 in the afternoon, with a super quick connection in Brasilia, it's not unlike what some of you guys maybe would experience in an airport like Panama or some of the airports where is designed to do a quick connection.

And so we're -- and it also with us -- keep in mind that it for the passengers, as well we're taking advantage of -- there is an compliance angle, 30 minutes to the airport. It's a quick check in, its a domestic check in and they do a pre-check of your passport and stuff, so that -- and then we have an expedited process in Brasilia when you do the quick connection.

But then also, we're basically capturing the demand from the middle of Brazil up, so those passengers don't have to come all the way down to Sao Paulo Guarulhos, they just kind of plug-in there and shoot up to Miami and Orlando and there's a lot of VFR traffic, there is lot of integration with Brazil from a family and small business perspective with South Florida.

So it's a line of -- it's not the core business traveler that would be traveling out of say Sao Paulo or maybe Rio up to those markets. It's also a different type of customer, which is -- which are business owners. And you know demographically using air travel, but it's a different targeted market in terms of this VFR traffic between South Florida and Brazil. And so that's a niche that where we've been focusing on in the context of having a competitive advantage in the operations from a cost perspective. And then of course on the other end in the case of Miami and Orlando airport we're helping Delta in terms of connections on -- quick connections onto other flights.

So when you get of the other end, there is a quick connection onto a Delta flight if you are connecting somewhere else in the Southeast of the US, as well as we're using, we're sharing infrastructure there in Miami with our partners, Delta to keep costs low, the check-in and the baggage handling and we have two maintenance employees in Miami, the extent of the Gol employees in Miami to meet maintenance, we're leveraging on our partners infrastructure. And so the breakeven load factors for us tend to be -- tend to be lower than the competition.

Q - Michael Linenberg {BIO 1504009 <GO>}

Great, that's very interesting. Thanks, Rich. Thanks, Kaki.

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

Thank you.

Operator

Next question comes from Roberto Otero with Bank of America. Please go ahead.

Q - Roberto Otero {BIO 16689399 <GO>}

Hi, Kaki. Hi, Richard. Thanks for taking my questions. The first one is a follow-up to Duane's question regarding Avianca Brazil. I know it's a situation not under your control, but what do you expect to be the most likely outcome from these ongoing negotiation with the lessors and the final say from the Brazilian judges. Also taking into consideration, why do you keep talk on (inaudible) first. And the second question is regarding models, if you could provide us the latest update regarding the ongoing process and the discussions with the independent committee, that's pretty much. Thank you.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

So thank you very much for the question. It is really hard to predict what is going to happen over the next step evolving this legal dispute. I believe that Cape Town is legally speaking in a sovereign issue and sometime I think that the lessors will need to get the planes back we will have access to that. I don't think that it might be anytime soon considering the news that we got from the press, I mean, how -- for the same source of information that you do have it's mine. But you know following our interpretation, our understanding on the legislation and we believe that the Cape Town agreement is sovereign in over any other legal aspect. And I think that sometime the lessors will get the planes, but it's really hard to predict at this moment.

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

Yeah, in terms of your question on the status of the discussions with the independent committee, Roberto, we're executing the process in line with the terms in form in the announcement that was made in December. We've been pleased with the level of expertise and professionalism exhibited by the independent committee in our discussions. And we're continuing to work with them constructively and cooperatively towards a transaction that benefits all shareholders. As soon as we have important developments, we will communicate them to the market as per the applicable legislation here in Brazil, but thanks for the question.

Q - Roberto Otero {BIO 16689399 <GO>}

No, thanks, Richard. Thanks, Kaki.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Thank you.

Operator

Your next question comes from Victor Mizusaki with Bradesco BBI. Please go ahead.

Q - Unidentified Participant

Hi, this is Paulo on behalf of Victor and we have two questions. The first one is, during the conference call back in October Gol's said that Smiles struggled to grow given our changes in the competitive landscape. However, Smiles reported a really good result in 4Q'18, this thing, how does these results change your view for Smiles'?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Yeah, hi. So, sorry, what's your name again, sorry?

Q - Unidentified Participant

Paulo.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Hi, Paulo. That was a great question, obviously our statement in the call on October as to Smiles structural growth challenges is a long-term perspective and not meant to address specific periods where external effects can impact and swing results one or the other. We think that in the Q4 -- last year in the Q4 as Smiles' management continues to do a great job including capitalizing on a market window that has recently been created by two specific scenarios. One is LATAM's ongoing process to acquire the floating Multiplus and as was mentioned on the previous question, Avianca Brazil's filing for judicial reorganization Chapter 11 here in Brazil, these situations created uncertainty around the business plan and long-term outlook for two Smiles' key competitors, LATAM's Multiplus program and ABB's, Avianca Brazil's legal program, this has allowed Smiles to capture disproportionate growth.

Yeah. I'd say two things I think are worth noting. One is that both of the situations -- both of these situations I just described while they create an opportunity for Smiles are actually long term consistent with our view that Smiles has a structural challenge to grow as a standalone entity as we mentioned in the October call that you're referring to. In the case of LATAM, we believe that a full integration of Multiplus into LATAM will place Multiplus in a structurally advantage position by completely aligning the interest of the program, the loyalty program and the airline. And in the case of Avianca Brazil's Chapter 11 filing and its effects on Amigo, we believe that that situation as highlighted the shared credit risk between airlines and their affiliated frequent flyer programs and that will make it more difficult for programs to finance themselves and their working capital on a standalone basis. So we're keeping our eye very close on the working capital situation of the loyalty program. The second thing that I think is worth noting is that highlighting the ongoing challenges of growth when you look at -- when you guys look at this in your analysis, when you compare historical performance of loyalty programs. Yeah, when you look at comparable periods you see that revenue growth came at the expense of substantial margin compression, especially at the net income level. And so in the case of Smiles even though gross billings grew nearly 20% and redemptions grew over 5% [ph] net income, excluding the one-time events which you analyze, they barely grew 3%.

So this trend relates to the curve and where we are in the cycle. But we continue to believe that the long-term growth and profitability for Smiles will be more and more challenging and the results announced by Smiles in 2018 don't change our view of the merits of the reorganization for both Gol shareholders as well as Smiles shareholders but thanks for the question, it's a complex issue and I think it merits some careful consideration. I think you said two questions or was that the question?

Q - Unidentified Participant

Thanks for the answer. For the second question, it's the three rejected your proposed structure to lease go at Nova Mercado and it would make sense to allowing offer for Smiles.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Yeah, as stated in October of last year, public offering and delisting tender offer remains as an alternative. But we still believe that a structure involving Smiles merger brings more benefits to and it is also better for Smiles' minority shareholders. And is this rationale that guys are in discussions with the independent committee.

Q - Unidentified Participant

Okay. And my third question is the press mentioned that the Conforto family would be Chile's control of Gol as part of the plan to lease Smiles and integrate the company and what's your view about these, so...

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

No, you are referring to a press article last week. I mean, it's highlighted in our notice to the market last week, the news in the press last week was produced without Gol's participation and it wasn't based on any concrete facts. And as we said in the notice, we strongly recommend investors not to make any investment decisions based on that news.

Q - Unidentified Participant

Okay, thank you.

Operator

The next question comes from Dan McKenzie with Buckingham Research. Please go ahead.

Q - Dan McKenzie {BIO 15071178 <GO>}

Hey, thanks guys. I have a couple of housecleaning questions here. First, what should we be putting our model for CapEx this year and next. And then separately as a housecleaning question is tied to debt at the Investor Day, I think you guys pointed out that the plan was to amortize roughly 2 billion in debt this year with free cash flow. And I'm just wondering what the average interest rate, the debt would be that likely gets retired here?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Yes, good questions. On the CapEx, we've provided you guys guidance on that this year, the operating CapEx of around BRL650 million a year and just to highlight that, that does not include aircraft CapEx for acquisition of new aircraft. We have sale leaseback '18 and '19 deliveries of the order to the extent that we would do, we'll start to do finance leases, where we would basically put in mortgage financing on those aircraft. We then could have some outflows from our own cash for pre-delivery deposits. But all of that -- all that aircraft CapEx, the airframe and the engine, as well as the PDPs is 100% financeable given a secured and unsecured mechanisms available to us. But that number is not in the CapEx, that is the CapEx, so the 650 we're providing there is the operating CapEx which is basically maintenance CapEx, engine overhauls, product enhancements, that's the guidance that we've provided there.

In terms of your second question, with the continued liability management that we're doing and the debt amortizations, our focus there is on the dollar side that's with coupons in the high eight's almost 9%. There's a little bit there, and then the remainder of that the big chunk of that is a combination of our Brazilian debentures, which it's a variable rate, but today have a rate of around 9% in reais and then some other financings that have been done for CapEx, which have the rates of kind of 5% to 6% in dollars.

So the net-net effect of that it's -- that it's going out has a cost to us in the income statement of around 8.5%, but we are today in a market environment in Brazil with interest rates of around or below 8%. And as you know, we've -- the bond deal we did in 2017, sorry 2018, 2017 December 2018 January has a 7% coupon and a part of the use of proceeds on that what we've been using to do this liability management on the dollar debt that have costs in the high eights to low nines. And so we are getting an interest savings there which I think where you're going to add which can impact earnings. On average between 100 to 150 basis points, on the liabilities that we're reducing is generating a reduction in interest expense cost of around 100 to 150 basis points.

Another way, I can say that is that as I think we've mentioned on calls in the past is that we're working to get the interest expense component on our business on the ex-effects of IFRS16, the interest expense on our balance sheet down to around 5% of revenues. And so one way you can also think about that is that we're targeting to get to roughly 5% of revenues, the overall interest -- outflow of interest expense on the business as compared to our revenues to be about 5% of the total and that structurally will be kind of where we want to get in terms of optimal capital structure. So that's another way I can tell you to think about it.

Now having said that, you guys have a little bit of work now to do, to redo models and projections in the new accounting standard of IFRS16. And so all of our numbers going forward, as of January 1, including the guidance we provided, the kind of update on guidance we provided today, that's on the new accounting format of IFRS16, so you'll see a net financial expense now for this year of BRL1.2 billion, that includes the aircraft lease components. So embedded in that number is the other interest expense, which today is only -- is in the range of BRL500 million in terms of what I just mentioned. And then the other BRL700 million is the interest expense component in the IFRS16 methodology on the lease contracts. That's something we can also talk about going forward as you guys adjust your models to the IFRS16 format, you have to make those adjustments including in the net financial expense line, which is we've represented that in the guidance that we provided this morning.

Q - Dan McKenzie {BIO 15071178 <GO>}

Okay. Thanks, Rich, that's very comprehensive. And then just for a follow-up question here, with respect to the economic recovery, you guys referenced, the recovery expected to be pretty even throughout the country or are there parts of the country where the demand backdrop is stronger parts of it where it's weaker, I'm just wondering if you might be able to sort of compare, contrast sort of the Sao Paulo Rio versus the rest of the country? And then just one other kind of big picture question at the Investor Day was I think it was pointed out that the structural reorganization of Smiles could improve margins this year. Just wondering what's embedded in the current outlook? And I'm wondering, with respect to the guide and I'm wondering if you can provide some perspective what that upside could potentially look like?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

So, we'll start by answering your question on the economics of recovery, that question gives me the opportunity to better clarify why you have emphasized so much our privileged position to make the most out of that movement. Being the market leader among the eight -- among the top 10 airports in Brazil, we have also a clear advantage in our offer to the business drivers. And these are the first ones to fly more and this is exactly what's going on right now.

So if you consider that this top ten airport, they are basically located in the South part of our country, and they together extend for more than 70% of the total traffic. It is likely that these positive demand at the beginning of this year has been generated by a much higher dynamic in the business segment. And therefore Gol has improved its results by capturing the largest portion of these customers was the combination of our network and the products that we have developed it around the last four years position ourselves at the highest position in their customer -- in the business driver choice to travel, choice to travel.

So now what we are facing, what we are finding in the market is a much higher level of business activities than we experienced in the beginning of last year and that's what is sustaining this higher yields. Personally, I believe this is a positive trend supposed to continue over the following months. So, Richard is going to comment on the Smiles structure on that, that you have asked.

Q - Dan McKenzie {BIO 15071178 <GO>}

Yeah, very good.

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

Yeah, I mean, I'm not sure if I totally got the question, Dan, but the -- maybe you can repeat it.

Q - Dan McKenzie {BIO 15071178 <GO>}

Yeah, no, industry date, I think it was just pointed out that the structural reorganization -- structural reorganization of Smiles could improve margins. And I'm just wondering if you can maybe provide a little bit more perspective around that, what if anything you might have embedded in the guidance currently? And what that potentially could look like post any any restructuring or post the restructuring?

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

Okay. I see, I see, yes. I mean there is nothing in the guidance related to an outcome on the peak end at this point as and it really won't, it won't have any impact on operations. The benefits that will come from that or combination of if you want the synergies or the, the pre-launch if you will, that gets eliminated you know comes out of better efficiencies on taxes or at goal at the airline operating company. We have $1 billion of NOLs, which today only compensated against profit at the airline post merger. The large amount of profits that are at the Smiles subsidiary in Brazil, they have to be compensated based on the tax idea of each individual company, you can't share them across group companies even though you control.

So that is a big source of cash flow and earnings once the merger would be effective, but we don't have any assumptions on that right now, the leakage if you will on just that item alone it varies, but it's grown to a rate of over BRL200 million a year. It's a combination of higher taxes on revenues that the Smiles subsidiary pays, as well as full income tax. And so those synergies are self-evident and only possible via a merger. And so once we, once we have an outcome of that, yes, that would generate some substantial cash flow, as well as earnings accretion and allow us to better manage our taxes and NOLs across the group. There is other synergies as well as Kakinoff mentioned on better optimize revenue management, better competitivity versus what our main competitors are doing. And then also as well cash flow that comes out of some other components as well. But as we said, that process is ongoing and it's not going to be a couple of months before we have greater visibility on that and we'll update you guys once we have greater visibility -- greater visibility on that.

Q - Dan McKenzie {BIO 15071178 <GO>}

That's perfect. Thanks for the time guys.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Thanks, Dan.

Operator

The next question comes from Pedro Bruno with Santander. Please go ahead.

Q - Pedro Bruno {BIO 19082978 <GO>}

Hi, good afternoon, thanks for the questions. Could you comment on what's behind the upward revision on the guidance in terms of margins or perhaps confirm my impression that it relates to the VAT tax cut recently announced by the Sao Paulo government, I'm talking about the 1 percentage point increase on the -- we can talk about the EBIT margin, that will be the first one.

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

Yeah, you're correct your impression is correct that comes out of a lower net price per liter for jet fuel, you saw it was revised down by around $0.10 per liter, and that's the change. The only change in the guidance was that which has had roughly a 100 basis point impact on our margins. And then the corresponding roughly $0.10 impact on earnings per ADS as was disclosed in the release that went out this morning.

Q - Pedro Bruno {BIO 19082978 <GO>}

Thank you, Richard. And then the second one if I can, if you can also give us a bit more color on what's behind the guidance in terms of jet fuel and Fx and of course you provide the jet fuel component but in reais would be interesting to have an idea of what's behind or would be the impact of the currency there perhaps talking in terms of average either FX or could be brent or WTI for 2019 versus 2018. that would be great. Thank you.

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

Yeah sure, yeah, we don't provide those numbers, because you guys in the markets come up with those numbers on estimates for currency and oil prices. And we use those averages in the data we provide to the market. Obviously, we work with other types of forecast here because those are, I mean, external inputs, dollars and oil prices and oil. Having said that, oil -- we basically through our combination of hedging and capacity management, we've taken the oil -- the upside oil risk of the payable. We're hedged on our 2019 oil fuel -- oil consumption, about 60% in the low 60s WTI and which would be kind of high 60s Brent. And so if we have a scenario of oil prices above that, we would be generating gains on our hedge portfolio. Of course the capacity dynamic allows us to have a fair amount of recapture or pricing power on to yields, which is buoyed by the very rational supply demand balance, as well as the excess demand, that's been coming into our domestic market as a result of a variety of factors.

But having said that, we here at Gol, we're bullish on oil based on our process and our forecasts, we expect oil at the end of this year above $70 brent and that's a reflection how we're approaching hedging. On the currency side, we're just using the same average as you guys work with, I think what you'll see in -- if you try to back into it from our numbers, you'll probably see something between 3.6 and 3.7 average for this year for currency in those forecasts, but feel free to use your own forecast for currency and oil into our -- the matrix of a lot of detailed metrics for -- help you guys do your models.

But having said that, historically, there is a very high negative correlation between oil prices and currency. And so if we do get an appreciation in oil, it's likely that we continue to get appreciation in the currency. But you guys are better than -- the best to come up with what you think the right Fx is to use there. The comment I would make on that is that our first line of defense on the currency is what we do on the revenue management side and our ability to have pricing power comes out of what's going on in the capacity side of the industry. Obviously, we're the largest domestic player, we have the biggest impact on capacity, but we have other competitors and lot of intense competition in the market.

And so the overall rationality of capacity in the market will ultimately determine how we are able to manage margins through any volatility we might get, say in a currency, if there is a rapid currency depreciation and our ability to adjust fares over the booking cycle. But is the depreciation of the -- or appreciations are normal, in other words, if the variation in oil price and currency is with normal volatility that's generally captured in the regular yield management. How we approach hedging here it's meant -- it's designed to protect us against the dislocations when all the correlations tend to go to one and then you've got a period of 3 to 6 months, we've got to manage through abnormal volatility.

But the key driver and the key thing that I encourage people to focus on and you see this in the monthly traffic stats for the whole industry is what the supply demand balance is in the local market. And historically when we have RPK growth in excess of ASK growth, in other words rational capacity, in our market here in Brazil and this is statistically significant data for the last 20 years in the market, which is as long as we've been operating in it. We have a 70% correlation of Brazilian yields with the US dollar. And so our yields are highly dollarized when we have a rational supply demand environment. So the key driver here to focus on for that is how well we're doing on that balance of supply and demand, that's ultimately going to determine, however everything else falls in line. But of course as you know, we do a lot of proactive hedging both in oil, as well as currency to buy sometime to adjust and ultimately, we're working to for a margin outcome.

And so the margin guidance that we provide to there is what we're working for across the board capacity management, revenue management, hedge management, it all works together in a coordinated way to help us achieve what we're guiding on margin, but not any one variable on itself isolated matters, but the most important variable is obviously the capacity. That's how I would answer that question and guide you guys in terms of how we're thinking about that in the management of our business.

Q - Pedro Bruno {BIO 19082978 <GO>}

Very clear. Thank you very much.

Thanks, Ped.

Operator

Your next question comes from Savi Syth with Raymond James. Please go ahead.

Q - Savi Syth {BIO 17476219 <GO>}

Hey, good afternoon. I was wondering if you could provide a bit of a color on the kind of the key cost items and how you're thinking about them in 2019 and 2020, that kind of drives your CASK ex guidance?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Sure, Savi, yeah, it's a good question, I think that the main way that we think about especially CASK ex-fuel at Gol is what we're doing on aircraft productivity and dilution of fixed costs, that's really our key focus here to go on the cost side, it's productivity. And so we're working as you've seen in the last many quarters, we've been consistently increasing our aircraft utilization, we're on our way back to roughly 12 hours a day of utilization, which for us here in our business is about 11 flights a day when you put in turnaround times and the maintenance is roughly 24-hour day operation. And so we're always working to try to maximize the productivity out of the aircraft in general.

And also this year, we're starting to get more of the effect of the MAXs' coming in and they have a higher productivity overall in terms of having a slight -- nine additional seats on the aircraft as well as a longer stage length. And so this year to next year, we start to get a little bit more of that effect where the capacity that we're putting on is coming out of this up gauging as opposed to adding additional fixed cost. And so we're getting better fixed cost dilution.

And so this year we are basically going to be achieving around 3% to 4% increase in productivity through that effect that I just described, which if you assume currency stability or appreciation basically covers us for inflation, in other words, the normal call it 3 to 4% -- inflation this year in Brazil is running and we've been running at all time lows kind of below 4%. So we basically have inflation covered with what we're working -- what we're achieving on the productivity side is a combination of just increasing utilization and then as well as the effect of the MAXs' coming in and the up gauging on the NGs.

And that effect will continue, we want to say like this year 3% and 4% next year, 3%, 4% that will continue as we transition the MAXs' into the fleet and that's pretty much across the board in terms of the non-fuel part of the equation, that's the real driver. Generally in Brazil, we have to deal with annual inflation and cost of living adjustments. So we're always dealing with the inflation impact on our costs. So the way that we're keeping these costs stable at this roughly BRL0.13 non-fuel CASK is out of that effect and it's structural and it's something with it obviously, we are working on many years as we've developed the MAX coming into our fleet. But just to make a comment that also impacts the fuel as well as you know because of MAX aircraft as you're probably seeing companies like Southwest and Ryanair in your coverage of US and European airlines, that we're getting the as advertised fuel economy on the fuel consumption of -- for us versus the 800, it's about 15% on a per ASK basis. And that's significant, especially, that's the biggest component of our cost structure. And what you'll see as you adapt your models now to IFRS16 with the moving of the -- with the full movement of the aircraft component below the operating line, the fuel component now has a larger weight, has a larger ponderation percentage if you will in the overall cost structure.

And so the fixed cost dilution is even more evident, but as is more important the fuel savings. And so that's how we approach it, it's real on these two angles. One is that, the productivity in the absolute lowest fixed cost possible and then a huge focus as well on the fuel management from an operating perspective to make sure that we're squeezing every milli cent out of -- out of that.

And those two components ducktail very nicely with the MAX coming in and the MAX is kind of like the perfect machine for us to operate that in terms of how we operate in our network. And that's probably what year ago we think about 95% of the day is those items that we are always working on optimizing that current projects, medium term projects always focused on that. And so that's -- that's basically our real house and that's where we think we excel at the source of our competitive advantage.

Q - Savi Syth {BIO 17476219 <GO>}

Okay. That's helpful color. And just -- just on that, is the payroll taxes reversed, is that not a meaningful impact and as we kind of think about the cost side? Hello?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

We've just lost the mic here. On the payroll tax, I mean that's been on the docket for a while, for that potentially to be reversed, keep in mind that it has an impact on revenues, as well as costs and there is a net effect.

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

Yeah, actually today you're not going to have it, but if the government has said they would like to -- for you to analyze the possibility of having a more comprehensive plan evolving more companies and sectors that should be that in a more stricter way. So at the moment, we are not considering anything, because you know the fiscal situation in Brazil is pretty critical and we cannot assume that this -- this is a sense that we will be -- assume -- it will be available anytime soon.

We might actually -- every year we budget that it's going to go away and always like the guidance we provide you every year last year I mean, every year we budget that it's going to go away. And so it's the effect of it going away in terms of the and we say go away, it has an impact both on net revenues as well as the cost, the costs go up, but then the net revenues will also go up a bit because of how it works. And so that net effect is in our guidance, but like you're saying is that, it's, I would say it's a 50-50 chance this year that it goes away or doesn't, but it's not in the first half of the year for sure definitely in the back half.

Q - Savi Syth {BIO 17476219 <GO>}

Got it. And just -- just a quick slightly longer-term question, as your balance sheet improves, I think the more strategic view on financing, is there a right mix of operating lease versus kind of debt finance aircraft right now, it's more heavily weighted towards operating leases, I was wondering if that would change over time.

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

Yeah, we are changing a bit, we're like in the first cycle, we did, which was the 80 aircraft we did of NGs which started arriving here in 2006 and that cycle is basically finishing now. We had a policy of -- we had a policy of (technical difficulty) somebody is catching a flight there. We had a policy of 50-50 sale leaseback, finance lease. And the concept there is the flexibility to get out of operating lease aircraft and our first phase was higher than the finance leases and that was evident i think in our 2015, 16 downsizing. As you know it's been a six-month period, we were able to reduce 29 aircraft, nine of them were finance leases and 20 of them were operating leases. And so we're able to get together with our leasing companies and make a quick adjustment, that flexibility is a little bit higher in an operating lease contract than a finance lease.

Having said that, in this next cycle which will happen over the next 10 years, which started in 2018, we're going to have a 135 MAXs. Our plan is to do 60% finance lease and 40% operating lease over the course of the cycle. And so that would be roughly 70 to 80 finance leased aircraft over the next seven to 10 years. And probably, Savi, in the third cycle which will be say 10 years from now whenever the new version of the Boeing 737 comes out, we'll probably be going to something like 80-20, 80% finance lease, 20% operating lease. But it's a little bit of our ownership mentality here where we'd like to take ownership of the aircraft, because you know some companies don't take ownership at all, including some of our competitors or the opposite, which is all ownership like you might see in Ryanair or Southwest where they have a high -- very 90% plus level of finance leases. We're still growing into having the majority of the fleet be owned and I think the MAX period for us will be that transition, but the '18, '19 orders if you see were sale leasebacks and part of that reflects the other component where we like to have our foot in both market is we can take advantage of the supply and demand factors for aircraft in both markets, in other words, this is a robust demand in the sale leaseback market, we can make money in that market and when not, then we can always count on the finance lease mechanisms, which have export credit guarantees and other mechanisms which are becoming more diverse in this next cycle.

And then we can have that kind of as a backstop, but -- so we like to take advantage of the supply and demand in both markets which happen over a longer cycle then in the day-to-day of just the pure airline transportation business. So it's another part of our business, it has a different dynamic more of a long-term. And we think we've been able to -- in the way we've done it in the policy of a part finance leased, part operating lease have been able to create a lot of long-term value and been able to unlock it when we've needed to lock it.

So a lot of it will end up -- we're done with all the dispositions of the NG portfolio, we will have realized you know around $500 million of gains on that part of the business, which came at a very important part of the cycle for us in kind of the trough, if you will of the Brazilian airline cycle which was 2016, 2017. And so what I'd like to say is that that provides -- that part of our business provide some nice downside protection for the business for creditors, as well as shareholders when we need to tap into it, but we did -- but it does take a long-cycle to build that up and worse finishing the cycle and the NG starting the cycle on the MAXs. And so that will continue to be an interesting component of the business over the cycle, but obviously it -- I realize it does create some challenges to try to project and predict it because we're taking advantage of the market. And we've had in '16, '17, '18, '19 a lot of our profits have come out of that and then we'll probably have a period of '20, '21, '22, where it will be the majority of the profits will not be coming from that all, this should be coming from the core demand in the airline transportation business. And then when we get to the other end of the cycle kind of 2025, '26, '27 we will have built out some substantial equity in the MAX portfolio and at that point in time if I'm talking to you on the phone we'll probably having a similar conversation about what we're doing with the equity gains built up in the portfolio then. And so it does create some challenges for those that are looking at our business with more of a short-term focus.

Q - Savi Syth {BIO 17476219 <GO>}

That's very helpful. Thank you.

Operator

The next question comes from Rogerio Araujo with UBS. Please go ahead.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Hello, good afternoon, thanks very much for taking my questions, Kakinoff and Richard. I have a couple, so the first one is a follow-up on your '19 guidance. And so if we exclude that 7 is back gain and also the demand and expenses that are one-off, your guidance implies a 6.5 percentage points margin increase year-over-year. And in our calculation this would imply between 6% and 7% yield expansion year-over-year for 2019. So my question is, does it make sense in our calculations and Gol expecting a significant expansion in ticket fares this year, if this is related somehow to Avianca Brazil's current situation or to a demand improvement, how you see your future bookings, so this is my first question regarding yields implied in your guidance for '19. Thank you.

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

Hi, Araujo, actually that's a mix of all the things I have just mentioned, we have a more benign market, we have some shift considered already from Avianca Brazil to ourselves and the economy is fastly or faster than other segments recovering in our specific segment. And you have also a higher penetration, they have market share in the business segment, which give us higher fares in comparison to last year.

So, definitely we are positive and more bullish regarding the market and mainly our performance, which might be benefited by the Avianca Brazil effect, but also a considerable portion of that and hence the performance comes from our own sales structure, revenue management strategy and mainly the product which has been considered by the business travelers as more attractive than any other player.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Yeah, one of the coverage area when you compare the '18 numbers to the '19 because the guidance numbers we are presenting now for '19 are in IFRS16 and there is about a 5 point increment in the new methodology. On page 16 of the release, we provided a table which shows the difference between 2018 as reported and what it would look like in IFRS16 and it's about a 5 point change on the operating margin. And so for example, the 2018 pro forma EBIT margin in IFRS16 was 17.6%. And so there is not and there are guidance for the 2019 is 18% in the same methodology. And so there's not a whole lot of increment there in the '18 to '19 (technical difficulty) is the -- you have the transitions now because that's how all the reporting is doing.

But yes, you are right that we are and we're seeing this, we are assuming yield and RASM, RASK growth, you know three -- two to three points above inflation. And so there is a big source of the -- of that is coming out of the underlying demand and the supply demand balances which is allowing us to continue to expand yields above inflation. And then also some of the effects I mentioned in the answer to Savi's question which is the increase in the productivity that we're seeing in there. The other -- the second main driver there, it's in -- and then margin expansion is the increasing utilization, the MAX is coming into the fleet and the better productivity we're getting on the fixed costs. And so all that is kind of driving that slight increase in the margin, but at the end of the day it's when you exclude extraordinary effects and so on, it's -- it's like a two point increase in margin, apples-to-apples '19 over '18.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Yeah, this is so -- let me go through this, again, sorry. If you exclude sale and lease back this and you -- if you also adjust it for the IFRS16, this would be about 7 percentage point increase year-over-year, is that correct?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

No, it's not correct. I think what you're mentioning there is like the effect of the -- when you talk about the asset management part of our business, the net effect on '18 is about BRL350 million, right? So that's about what three points of margin and so that's the number if you wanted to kind of back it out, you could back out three points of margin from '19 if you wanted to do that, but we manage one business. And so that -- that's how we manage the business as I was saying, we don't -- how we get to the margin is a function of how we manage all of our businesses. And we have a lot of flexibility on how we can manage those. And so, yes, if you were to, if you wanted to exclude a number from '18 related to the asset management part of our business, it's about -- it's a little over 3 points of margin. And so that's a number that you should use them to maybe make your calculations in the context of '19 and the real growth and margin.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Okay, it sounds good. I'm going to be happy if you can -- if you can discuss this later, (multiple speakers).

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Yeah, sure. No problem because -- no problem at all.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Yeah. Thank you. So the second point is that the financal above CapEx, if you include that into your guide -- if your CapEx for -- if your guidance for CapEx, how much would like in 2019 and maybe 20 and so including financial above CapEx, how much would it be in '19, '20. Thank you.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Including financial CapEx and in IFRS.

Q - Rogerio Araujo {BIO 17308156 <GO>}

So if you include 1% of the CapEx is including the aircraft that you were going to receive and do financial leases, if you include everything, how much would be total investments in 2019, that's the question. Thank you.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

All right, well in 2019, we don't have any financial leases. All of our '19 deliveries are sale-lease back. So I'm just trying to understand your question, identifying your question, Rogerio.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Okay. You said that your CapEx guidance for 2019 and '20 does not include CapEx for acquisition of new aircraft and...

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Okay. I got, I understood, understood you said yeah. What I was trying to say there was the following is that we have been in the first part of our orders, it's -- that CapEx there is what we call kind of operational CapEx or maintenance CapEx, product CapEx, that's the number that we're guiding there. The decision on the fleet financing, you'll know that when we do it. And so what I was just saying there was that, for example, if we end up doing, for example, some finance leases on the back end of 2020, we basically made decisions on all of our aircraft deliveries until the second quarter of 2020. And when we do that for example, if we're to announce a finance lease package for a number of aircraft, say five aircraft, then that would create an aircraft CapEx, which would then be financed with secured and unsecured financing. We haven't made the decisions on those yet. And so when we -- so no decision on that in those 2019 or '20 numbers. If you just take the PDP component of if we were to go between you know between half and a 100% of our deliveries in an individual year in a finance lease format, that's anywhere from $50 million to $75 million of outflows for PDPs. But keep in mind that how we do the financing on the aircraft, it basically gets to pretty close to 100% LTV. And so when the aircraft CapEx is enormous, it's in the billions, over the life of our order, it's all 100% finance. And so you would see a number for CapEx coming in through the aircraft acquisition, but it's all 100% finance, with secured and unsecured financing. So it doesn't generate any cash outflow for us.

And so the way we are providing the guidance is you can understand what the underlying CapEx that's required for the airline operations business, but it really doesn't relate to the aircraft financing cycle. Also because we have not made any decisions yet with respect to finance leases. We do expect to make these decisions between now and September. And so I think by September of this year, we'll provide some visibility on what 2020 and 2021 will be looking like from an aircraft acquisition perspective, but right now, we haven't made any decisions on that. So it's hard for me to guide on that, because we can also end up in a format where we keep doing sale leasebacks for '20 and '21 in which case none of this would flow through that, will flow through that line item. But it's all a 100% financeable with low cost sources of funds, generally in the secured component of our aircraft financing, where we're getting 12-year money at 45% cost of funds, all in.

And then we complement that with a little bit of unsecured financing, which ends up having a blended cost of kind of 5% to 6% with an average maturity of around 10 years. So it's a very well organized finance part of that business, which doesn't generate any pressure on our liquidity management in the business.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Thanks very much.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

That's good question. Thanks.

Operator

The next question comes from Petr Grishchenko with Barclays. Please go ahead.

Q - Petr Grishchenko {BIO 19084897 <GO>}

Hi, good afternoon and thanks for taking my questions. I guess I wanted to follow-up first on Avianca discussion. There are some conflicting reports on what could happen to Avianca capacity particularly to (01:21:44) and some major airports. So maybe if you could outline kind of scenario so how you think the market could evolve if let's say Azur or LAT air capture this capacity?

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

I think actually I wouldn't like to speculate on possible scenarios because we are talking on a competitor which is fighting to go through the situation and we have no intention to consider, it's because these scenarios because we would like to drive the public opinion nowhere, but is to follow what's going on and try to understand how the market will naturally accommodate around this situation, because actually nobody know. I mentioned before that there is this legal dispute and the Brazil has acquired robust legal system, but unfortunately at this moment, this lack of visibility of clarity raised several speculations regarding its laws and possible outcomes in the -- at the most congestion airport.

I think that those were the less where Avianca Brazil would give up on it's current footprint. So I mean that we would possibly see a much lower capacity of Avianca Brazil in the market before they would give up on the slots that would significantly change the landscape in the airline segment in Brazil.

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

Yeah, we feel that the January data, Petr, which is public, I mean ABB had a reduction of domestic ASK 7% to 10%, negative reduction minus and that company had been growing at around 12% run rate on domestic ASK increase. And so if you take the delta on that versus expectations, it's almost a 20% reduction in the run rate capacity growth of that company. And that's just based on the data, the traffic data, the public data that's out through January, so that might be one way for you to think about how that can be impacting the overall supply-demand in the market. Then as Kaki said before, we're not changing our domestic capacity plans for this year. We do have the flexibility because we operate one aircraft type on one unified network. And so we can shift capacity between domestic and international and we're always working to maximize the overall profitability of the network with a capital, the network, one network, including the international, so one asset, if you will. And so we can adjust capacity based on where we can get the best profitability on the allocation of our aircraft over the full network. And so we have a lot of flexibility to do that, but we also don't see in the market anybody changing their capacity plans based on what's going on. Having said that, we are experiencing now a phenomenon that we haven't seen, maybe you have to go back to -- I don't know, maybe we have go back to like 2010 to have an excess demand environment which is what we are living in now, but that also relates to the overall airline cycle which has nothing to do with the comings and goings of anyone individually.

And remember that as well, I mean, we are also dealing with the demand environment, that's the most powerful component that is found. The capacity environment is helping and we've been working very hard over the last three years to get to where we are in capacity. And we feel like we're in a good position with the combination of the market as well as fleet plan to flex around whatever is going to come our way over the next year or so.

Q - Petr Grishchenko {BIO 19084897 <GO>}

Got it. Very helpful color. Second question, I mean I appreciate your comments on financing, they were very helpful, but looking at your amortization schedule for this year looks fairly smooth, is there any expectation that could access either international or local DCM this year?

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

Well, no, we don't -- I mean, we've already done everything we want to do an unsecured debt. Most of our work going forward is going to be unsecured debt. Having said that, we are running airline and we're always going to look at where we can opportunistically improve our balance sheet, but anything we would have to do would have to -- have a lower cost of capital than the liabilities already in our balance sheet or it would have to have more of a component, which would improve our credit ratios.

So right now we don't see anything in the international unsecured debt market that would meet that. As you know, also (inaudible) interest rates now are record lows. The issue is the tenure, it's hard for a company like us in the domestic market to raise money beyond three years, but money is available to us today in the Brazilian market at around 7%. And so some of the stuff that we're looking at it tends to be more on the shorter end, on the working capital, but it's starting to become more optimization on the pure debt side than on the -- than on structural because our 2025 maturity basically covers us. So, everything we want to do as it relates to aircraft acquisition. And we've been using that to clean up everything we can in the liability management side, the only thing we have left over is the 2022 as we have a call (01:27:44) next year and then the term loan, which we plan to amortize in August of 2020. But of course, we'll always see -- we'll always look at things opportunistically as a way to either improve our capital structure, equitize our balance sheet or improve our credit ratios in line with our ultimate objective to get back to double BB minus -- BB minus credit ratio.

Q - Petr Grishchenko {BIO 19084897 <GO>}

Perfect, thanks a lot and best of luck to you guys.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

Thank you.

Operator

Excuse me, this concludes today's question-and-answer session. I would like to invite Mr. Kakinoff to proceed with his closing remarks. Please go ahead, sir.

A - Paulo Sergio Kakinoff {BIO 5160310 <GO>}

So I would like to thank you all and incentivize whoever is considering to come to the Brazilian Carnival, we do have quite attractive fares to the biggest party of those, so have a nice holiday, thanks so much for you attention, bye bye.

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

(foreign language)

Operator

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