

Conference Call
Azul
2Q18 Earnings Results
August 9, 2018

Operator: Hello everyone and welcome to Azul's 2Q18 results conference call. My name is Roberta and I will be your operator for today. This event is being recorded and all participants will be in a listen-only mode until we conduct a question and answer session following the Company's presentation. Should any participant need assistance during this call, please press *0 to reach the operator.

I would like to turn the presentation over to Andrea Bottcher, Investor Relations Manager. Please go ahead.

Ms. Andrea Bottcher: Thank you Roberta and welcome all to Azul 2Q earnings call. The results that we announce this morning, the audio of this call and the slides that we will reference are available on our IR website.

Presenting today will be David Neeleman, Azul's founder and Chairman and John Rodgerson, CEO; Alex Malfitani, our CFO and Abhi Shah, our Chief Revenue Officer are also here for the Q&A session.

Before turning the call over to David I would like to caution you regarding our forward-looking statements. Any matters discussed today that are not historical facts and particularly comments regarding the company's future plans, objectives and expected performance constitute forward-looking statements.

These statements are based on a range of assumptions that the company believes are reasonable; but are subject to uncertainties and risks that are discussed in detail in our CVM and SEC filings.

Also during the course of the call we will discuss non-IFRS performance measures, which should not be considered in isolation and are described in detail in our earnings release. With that I will turn the call over to David. David.

Mr. David Neeleman: thanks Andrea welcome everyone and thanks for joining us for our 2Q earnings call. As always I would like to start by thanking our crewmembers who work hard every day and provide our customers with the best travel experience in the industry. I am extremely pleased to report that we continue to run the best airline operation in Brazil. We remain the most on-time airline and we have recently

received several awards attesting to the excellence of our customer service. For the eighth time in a row we were awarded by SKYTRAX the best regional airline in South America and also the best airline staff in the region. We were also recognized by consumer.gov for having the highest standard of customer satisfaction and fewest customer complaints.

Each time I fly Azul I get more excited with the enthusiasm of our crewmembers; the quality of the service, which I think, goes really well for our future growth opportunities.

As you know we are going through a fleet transformation process by adding larger jet, next-generation aircraft. We are extremely fuel-efficient and have lowest trip costs. That is also the best way to combat the fuel and currency headwinds we saw in 2Q. This is why we recently announced an additional order for 21 E2s increasing our total firm orders for this type of aircraft to 51.

With the need to replace all of our current E1 aircraft this order guarantees that Azul will have the newest, most fuel-efficient fleet in the industry with the lowest CASK and the lowest trip cost, which is an unbeatable combination. As you know our A320neos have 56 extra seats compared to the E1s with a similar trip cost contributing to a CASK reduction of 29%.

The E2 story is very similar. It has a lower cost of ownership, less fuel burn, lower maintenance costs, and increased revenue potential from 18 additional seats. This results in a CASK reduction of approximately 26%. This results in a CASK reduction of approximately 26%. Moreover, the E2 has a trip cost that is 14% lower than the E1. So we are basically getting more seats for free and paying much less for each flight, which is astonishing.

Because the cost and revenue benefits of the E2 over the E1 are so significant it makes total sense to aggressively remove the E1s from our fleet earlier than planned. I have set an ambitious goal for our team to have this portion of the fleet transformation completed by the end of 2021. We are working hard on it and we will share more details with you soon.

This is absolutely possible because the E1 to E2 transformation process is significantly easier for Azul as it has the same type of... for our pilots. So our pilots can fly both aircraft at the same time. It is just plug-and-play. Our first E2 is scheduled to arrive next year, in June next year. We will start seeing this margin expansion benefit from this fleet type.

In summary we continue to focus on our margin expansion plan that we have communicated the market. We are well on our way to building a better company for our crewmembers and our customers and our shareholders.

With that I will pass the time to John to give you more details on 2Q results.

Mr. John Rodgerson: thanks David hello everyone. I also want to start by thanking our crewmembers for all their hard work during the past quarter. As you can see on slide five our adjusted Ebitdar increased 11% in 2Q and we recorded adjusted net income of 238 million, a record for a 2Q.

Our operating results were impacted by the 20% increase in fuel and the 12% depreciation of the BRL. Excluding special items related to the sale of six E-jets and the truckers strike operating margin totaled 3.7% compared to 5.8% a year ago. We grew capacity by almost 19% in 2Q while also expanding our top line by 20.5% and our Rask by 1.6% on adjusted basis. Even with a 20% increase in fuel and the 12% devaluation of the BRL total CASK increased only 3.9%. Cask ex-fuel was basically flat and on an exchange rate neutral basis would have fallen 5.1%, a strong indicator that our fleet transformation strategy is working as expected.

As David mentioned in the beginning of the call our decision to replace older planes for more fuel-efficient aircraft makes even more sense in the current environment. The A320neos represented 24% of our total capacity in 2Q and will account for 30% by the end of the year. The E2s coming next year will help us accelerate the fleet transformation even further.

Moving on to slide six you can see that fuel and currency had a negative impact of approximately 160 million in our 2Q operating results, which represents almost 8 margin points. Thanks to our margin expansion strategy and the ability of Abhi and his team to recapture revenue we recorded a recurring operating margin of 3.7% recovering six of the nearly 8 margin points. We offset 85% of the fuel and currency headwinds during the seasonally weakest quarter of the year.

Moving on to the revenue performance on slide seven we continue to benefit from a healthy demand environment and robust ancillary revenues. Considering that our average stage length increased 13% in 2Q our Rask adjusted for this increase rose 8.1% YoY. Our network advantage allowed us to grow capacity by 19% while increasing our average fares by 16% at the same time maintaining a stable load factor. Once again we increased capacity, yield and Rask at the same time. This shows how much we needed a larger aircraft in our network.

Moving on to slide eight our loyalty program Tudo Azul maintained the strong growth pace for 2Q reaching almost 10 million members. Gross billings ex Azul went of 38%

YoY with the majority of this increase coming from Tudo Azul Club and our banking partners, further increasing our share of the Brazilian loyalty market. We now have 18% gross billing share, up 14% just one year ago and still well below our fair share of the market. Unlike other airlines in Brazil Tudo Azul is wholly-owned by the company and this means that we have no tax inefficiencies and benefit 100% from the cash flow generated by this high-growth, high margin business.

On the right side of the slide you can see the cargo business is also performing extremely well. Revenue increased 64% YoY mostly driven by the larger cargo compartment of the A320neo and the growth of our international capacity. We are excited to deploy dedicated cargo planes next quarter. Clearly our cargo team earned the right to get these planes into our network.

Moving on to the balance sheet on slide nine I am proud to report that we ended the quarter with a solid liquidity position is of 3.8 billion BRL representing 45% over LTM revenues. Even with a 12% depreciation of the BRL we ended the quarter with leverage at 4 compared to 4.5 in 2Q 17. We use the industry standard of an adjusted net debt/Ebitdar was capitalized... 7x and includes all of our debt.

This result reflects our decision to hedge 100% of the principal and interest payments... 400 million USD denominated-bond issued in 2017, protecting ourselves against currency risk. At the end of 2Q this currency swap was recorded a net asset of 210 million BRL under the long-term derivative financial instrument. Alex, our CFO, deserves all the credit for this hedge.

Our low FX exposure is reflected on slide 10. Only 32% of our balance sheet is denominated in USD and virtually all of our working capital there is denominated in local currency. Additionally as you can see on the right side of the slide we continue to be long dollar. Our assets denominated in foreign currency, namely our cash, deposits and maintenance reserves abroad and our investment in TAP, surpass our dollar-denominated liabilities - and that is excluding aircraft, engines and spare parts, which are stated to the exchange rate every quarter and are also priced in USD. For this reason in times of weakening currency we are not nearly as impacted as our competition. This reaffirms our position as the airline with the strongest balance sheet in Brazil.

Moving on to slide 11 the moving currency and fuel represent an increase in costs of 8 to 9 hundred million BRL in 2018 representing a swing of up to 9 margin points; however as you know we have a multiyear margin expansion plan. Also we continue to see positive demand environment backed by the strength of our unique network as you saw on our July traffic release. Therefore we are confident that we can offset

most of these headwinds as a result of projecting an operating margin of 9 to 11% for 2018 excluding the impact of nonrecurring events.

We also think it is prudent to revise our capacity growth range to 16 to 18%, down slightly from 17 to 20% by making adjustments in both our domestic and international networks. We continue to replace older generation aircraft for A320neos, which as David mentioned are key to combat rising fuel prices and the weakening of the BRL. As a result we expect CASK ex-fuel to decrease between 1 and 3% YoY even with a devalued currency. Our plan of having a five-point margin expansion to 15% from the time we went public has not changed. Before the devaluation of the BRL we were ahead of schedule. We are still on track and still confident that the pillars of our margin expansion plan are working just as expected.

With that I will turn the call over to the operator for Q&A.

Q&A Session

Operator: ladies and gentlemen thank you. We will now begin the question-and-answer session. If you have a question please press the star key followed by the one key on your touchtone phone now and if at any time you would like to remove yourself from the questioning queue please press star two.

For those following the call via webcast you may pose your questions on the platform and they will be either answered during the call or by Azul investor relations team after the conference is finished.

Our first question comes from Savi Syth, Raymond James.

Ms. Savi Syth: good morning. I just wanted to follow-up on the revenue environment, which seems strong and I was wondering if you can talk about that. I think it was really strong before the truck drivers' strike and maybe a couple of weeks after strong, but then weakened.

I am just curious what you are seeing today. Clearly you had a good recovery in fuel in the quarter and I was just wondering your thoughts on how that is continuing and if you can give a little bit more clarity and color on domestic versus international that would be great thank you.

Mr. Abhi Shah: Savi this is Abhi here. So yes you are right. I think we started 2Q in April with a strong demand environment combined together with really good fare and capacity discipline. Of course that was interrupted by the strike and then the World

Cup; but we have seen a good recovery after the end of the World Cup, July recovered nicely at last through the three weeks there and we had a very, very strong start of August.

So I feel good about the demand environment I am seeing. Fare discipline is also very strong and I have said this before. I think the capacity environment and the fare environment are the best I have ever seen basically and so I think that is really setting the industry up nicely for the second part of the year.

So July traffic was strong, we had good domestic and good international performance as well. Domestically corporate and agency demand is what is driving most of the pop and YoY revenue and I expect that to continue. When we had the strike and the World Cup we sort of expected there would be some repressed demand, we experienced that with the previous World Cup as well. So I feel like that is coming back nicely on line for the second half year, which is seasonally the best part of the year. So I feel good about domestic coming back strong driven mostly by corporate, by agencies and by closing demand.

On the international side is steady as he could see on our traffic release. Probably the one soft spot is Argentina, where luckily for us we have lower exposure to the three daily flights at most and so that we are pretty well hedged against that. Europe is doing well and the US is steady; nevertheless we have made some capacity adjustments for international for the second part of the year. Between August and November our international capacity is down 12% just to be prudent given the currency and the fuel situation; but overall I feel good about it and I think domestic is really going to come back strong in the second half of the year backed by a good fare and capacity discipline.

Ms. Syth: that is helpful and on the domestic moderating growth as well; any color on the type of market... In that growth?

Mr. Shah: also between August and November we are going to cut our domestic by 5%. Basically for the entire period overall we are cutting 7% of capacity, which takes our guidance... Really I expect capacity for the year from something very close to 20 to something very close to 17 for the whole year.

It is a mix of domestic and international. Domestically it is a market that are obviously not doing well on a P&L basis, number one; it seems that are not in and out of our hubs, so any market that overflies a hub or underflies a hub is probably the first to go. So markets primarily outside our hub.

And internationally for example we are getting the daytime Fort Lauderdale flight keeping the night flight only in reducing some frequency in the Northeast of Brazil to

Florida. So it is anything that is sort of not-core to our hub strategy that is what we are cutting.

Ms. Syth: very helpful thank you.

Operator: the next question comes from Michael Linenberg with Deutsche Bank.

Mr. Michael Linenberg: guys it is actually Matt on for Mike. How are you? You mentioned that your capacity in Brazilian domestic market was the best you had seen in a decade. If that is still the case any rationale or aggressive action on capacity or pricing front domestically?

Mr. Shah: hey Matt I feel good about capacity to be honest. I think that... I thought about this before and there has really been a structural change I think in how airlines in Brazil are allocating capacity. We are not seeing airlines going after each other; we are not seeing them chase each other in markets that frankly they should not be in and they really do not have any chance to make money. I think airlines are focusing where they are strong and where they can make their network stronger. We will certainly be doing that with the A320s and you can see in our traffic we are putting them in our network. We are seeing great traffic growth, connectivity growth and I think we have set an example to the market how to allocate the capacity where it makes yourself better, and I am seeing that across the board and airlines really playing where they are strong. So I think that is a very, very positive sign for the industry and I think it is a structural change from what we had a couple of years ago.

Pricing as well I think whether it is fares or ancillary I see airlines taking advantage of the opportunities showing discipline in the market and really looking forward to taking advantage of the good demand that we usually have in the second half of the year.

Mr. XXX: just to highlight if you take a look we were actually down in departures in 1H of the year, -2%. So it is really the upgauging the fleet transformation and getting these new assets that have more seats, utilizing them 14 hours/day reducing our CASK; and so it is the right type of growth that you would want in our existing market that has been stimulated. Once again Abhi continues to increase capacity and expanding RASK. That is really a powerful combination because of what we are going to see on the cost side.

Mr. Linenberg: great and just to follow-up: what kind of impact are you seeing if any from the upcoming Brazil election on either business or leisure traffic in 3Q? Anything you can quantify or...

Mr. Shah: as I said before the demand right now is strong. I would say it is a little bit early to see the effect of the elections; it is going to be towards the end of September

and mostly October. So I think we will know more when we get closer. It is a distraction clearly; but at the same time I think we also have some repressed demand from the strike and the World Cup. So right now we are seeing good trends I think because so much of it is corporate that tends to be closer and we will have a much better idea as we get closer to October.

Mr. Linenberg: thanks guys.

Operator: the next question comes from Renata Faber with Itau.

Ms. Renata Faber: hi thanks everyone for the call and congratulations on the results and thank you David for talking about economics of the E2. If I am not mistaken I believe this is the first time you talked about that and there is plenty of interesting information on what you said.

So I am sorry to ask you to repeat; but could you please talk again about how the E2 will help Azul increase margins?

Mr. Neeleman: sure. Thank you very much. I will take that question because it is a real passion of mine and I think I have got E2 right now and I am really excited about it. This math is really pretty simple, it is not difficult. We have got a lot of our E2... E1s during crisis times, during 07 and later and we did not have the credit that we do have today and so we ended up paying a lot for these E1s particularly on sale leasebacks and financing.

So now we have a whole different situation with the company and so we have bought the E2s, the financing is less; the plane is at a very attractive price and so the first category is we have a lower cost on the airplane by a significant amount, so that is number one; then number two these new E2s have new generation engines on them and the fuel burn savings is... Absolutely as fuel is going on it is like 13%, 14%. So that is absolute... That is it.

Then you move to maintenance. We have a better deal for the engine maintenance than we do currently and so that is a big portion of the maintenance cost; the seat inner rows are longer, maybe have this period of warranty and a kind of maintenance honeymoon that goes on for up to five years and so our maintenance costs will be significantly lower - permanently and not just in the first five years.

And then we got 18 additional seats and so with the high load factors we have, we assume that we sell half of those seats and have a price and come up with a number, we add all that together and... magically be able to snap our fingers today and say if all our 63 E1s were E2s and we had those flying today we believe that that difference in margin is an astounding number, it is 9% difference of margin, 9 margin points. So 9 margin points over where we are today.

Now obviously things can change as far as fuel price and all that kind of stuff; but I am saying today apples to apples what that airplane will be our cost by airplane versus what we have today it is 9 margin points. That gives us a tremendous amount of flexibility and cushion. Obviously even if it was 5 margin points or we were able to lower fares stimulating more traffic; or fuel spikes up and we have got those most fuel-efficient planes in the industry; if the BRL is weak and we have a plan that costs us a lot less money and we are spending less money on maintenance, which is USD denominated.

So that is why I push the team. If it is imperative whatever we have to do we have been working very close to Embraer to speed up the production to have them coming in sooner and that is why we set this target to have all of the E1s gone by the end of 2021 and we will start to see that benefit next year as the planes start arriving in June. So I could not be more excited...

Mr. Rodgerson: ... he has been here all week driving us crazy...

Mr. Neeleman: I told them I have not sold a single share of stock and why would I when I see that coming? So am very excited about it.

Mr. Rodgerson: we are going to work to try to accelerate this. It is a very exciting thing especially kind given the additional seats, the lower fuel burn; we got a great price from Embraer. So we are very very excited.

Mr. Neeleman: it is amazing what we will be able to do in spite of our costs on the E1 really. It is remarkable that this team has been capable to pull this off. When we kind of get all of the assets and then we have got the NEOs coming too on top of that. So very exciting news.

Ms. Faber: okay thank you.

Operator: the next question comes from Dan McKenzie with Buckingham Research.

Mr. Dan McKenzie: hey good morning thanks guys. Corporate business is good. I am wondering if you can talk a little bit more about the leisure side of the business. So on the one hand it is seasonally exposed time of the year for leisure traffic; on the other we had some pretty sharp swings in foreign exchange and truly that impacted that part of the business.

So I guess the question really is twofold here: first to what extent was leisure demand impacted by moves from foreign exchange to the extent that we can pull that out? And then secondly how long does it typically take for demand to typically return?

Mr. Shah: hey Dan it is Abhi here. So overall Azul historically has been pretty small in the leisure market and the reason has been we have not had the right airplane to really have a big position in the market. We are starting to now with the A320neos. We are 15 NEOs today but 4Q will be 30% of our capacity will be A320s.

So what is happening with the Neos is twofold: we are putting the Neos in our network really connecting our hubs, so Campinas to Recife for example; Salvador a little bit, some were able to enter some leisure markets like Fortaleza, where historically we have had very, very low presence.

We are obviously seeing a very good market reaction to that. We are seeing unit revenue reductions much less than what we had talked about on the IPO roadshow, sub-10% compared to a CASK reduction of 29 and so a part of this is leisure demand, we were able to access that type of demand we did not have before; we were able to stimulate local demand out of our hubs whether it is Campinas, whether it is Belo Horizonte or Recife.

And we were able to drive a lot more connectivity in our network. To give you an example when we put in all A320s between Campinas and Recife we had an increase of 77% of connecting traffic, because it is not just leisure that are using this airplane and these routes; we have 50 destinations on one side and 40 on the other. The route VCP - Recife has 500 different O&Ds that flow over that route. The route VCP – Belo Horizonte has 800 different O&Ds.

So there is leisure demand helping us with this airplane; but it is also the base of our network, the breadth we have and the platform that is really strong. So I would say that because we have so much connectivity I think we are seeing good results for the A320 with some local-stimulated leisure demand, we are also driving incredible connectivity through our network. Does that make sense?

Mr. McKenzie: yes I understand and I guess a follow-up to that Abhi: what is the biggest leading indicator for leisure demand? Is it simply commodity prices or is it some other measure of employment or commercial activity? I know it is kind of a smaller part of the business; but as you think about turning on this part of the business what are the leading sort of indicators that you will look at?

Mr. Rodgerson: Dan this is John. The exchange rate devalued quite a bit; but the mood in Brazil is actually very positive. If you go back to 2015, 2016 when the impeachment was going on people were fearful of their jobs and that is not the case right now. There is good underlying demand, people are traveling, companies are hiring.

The fear was in 2015 and 16 “I might not have my job tomorrow” and so leisure really dried up and corporate also dried up. It was a completely different feeling we are seeing right now in the country. It is just a different vibe. Of course the exchange rate puts pressure on some international flying, go to Disney World and some things like that; but it is not nearly what it was before and there is actually good underlying demand in the country.

Mr. Malfitani: I think Dan - this is Alex - when we look at business confidence and consumer confidence I think those are good indicators of underlying demand. The trend in unemployment I think is important. Unemployment is we believe still high but it is trending down slowly and I think that helps consumer confidence right? It is a very different story for you to decide to take your family to Florida if you think you are going to lose your job.

But if you are feeling pretty confident that you are going to keep your job and you are going to have a decent level of income is cheaper to fly to Florida actually and spend your vacation there than to sometimes spend your vacation down here; and it is also cheaper to buy whatever you want to buy in the US right?

I mean I am an iPhone user, I have a few iPhones but I have never bought an iPhone in Brazil and for me to buy an iPhone in Brazil the exchange rate has to go to 7, and until the exchange goes to 7 it does not make sense for you to buy an iPhone in Brazil, you buy it in the US; by just flying to the US and buying your iPhone there you pay for the price of the ticket.

So that is what is happening. Obviously it is more expensive to go to Disney World with an exchange of 3.80 than 3.20; but if you are feeling confident about your prospects I do not think that affects your decision.

Mr. McKenzie: that is a great perspective thanks guys.

Operator: the next question comes from Victor Mizusaki with Bradesco BBA.

Mr. Victor Mizusaki: hi. I have two questions, the first one with regards to the losses with the E1. Is there any risk of additional or the risk of potential liabilities that can show up with the replacement, the full replacement of the E1 by E2?

And the second question with regards to your guidance. When you take a look at your guidance for CASK ex-fuel for the full year you were talking about a reduction of -1 to -3%; but YTD it is like 0.6%. So this big reduction in 2H is it just a matter of the introduction of the A320 or is there anything else here?

Mr. Malfitani: Victor Alex here. I would not call it risk; because as David mentioned the replacement of E1s for Neos or E2s is very positive. There may be an accounting

effect from selling aircraft at a different price from what is carried in our books; but these six E1s that we sold we actually generated cash because the market value of the aircraft was higher than the debt value that we had outstanding. So we generated cash and that is going to generate all the benefit in additional revenue and reduced costs that David explained.

So we are going to continue to look for opportunities to remove E1s from the fleet and accelerate the entry of E2s and Neos and if there is a book impact to whatever we do we will call it out as we did this time; but like I said it should definitely be very beneficial, a very accretive decision in terms of P&L.

Mr. Rodgeron: and we understand that the faster we get there the more competitive we are and margins go up significantly and that is why David is kind of going crazy in Brazil this week. Move faster, move faster; because he understands that the quicker that we can replace... David mentioned it but I want to highlight it; we are paying for some of the sins of the past, which was being a startup airline in Brazil during the financial crisis flying E1s and that was not a very liquid asset; and so that was naturally all going to go away over the next three to four-year period; but David is just saying hey, let us bring it to the last guys faster.

Mr. Malfitani: and on CASK guidance Victor it is really both the new E2 and the new Neos that are coming in 2H but also the run rate of the Neos that we took before right? So like we said we have 14% of ASK coming from next-generation aircraft in 2017 and we are going to have 27% this year; but in 4Q it will be closer to 30% right? So you have all of the third of our capacity coming from next-generation aircraft in 4Q, which has a much lower CASK than what we used to have in the past.

So that is where we are going to see the reduction in carry - and that is already happening right? We talked about the total CASK reduction that we would have had adjusting for FX right? So FX kind of clouds the benefit we are getting from the Neos; but once you adjust for that you definitely see a huge reduction in CASK from the next-generation aircraft.

Mr. Mizusaki: okay thank you.

Operator: the next question comes from Bruno Amorim with Goldman Sachs.

Mr. Bruno Amorim: hi good afternoon. I have just a very quick question on the price of jet fuel. WTI is up by 40%, as you showed in your release FX depreciated by 12% and even so the price of jet fuel per liter rose by just 20% in this quarter. So I just wanted to understand to what extent this fuel price was impacted by fuel hedges and what to expect going forward in a scenario of stable oil price and FX as the hedge currently in place remains less relevant, thank you.

Mr. Malfitani: sure. There is a number of different factors all of the same time. So we do have some direct hedges with Petrobras. We essentially predetermine the price of fuel we are going to pay ahead of time and when we buy that fuel we pay the upon agreed price when we hedged it.

You saw in our traffic release and you can see on our ASK the mix of international flying is going up significantly. There is no ICMS on international flying and so that mix shifts more fuel consumption to fuel price per liter that does not have the ICMS burden. So that affects the blended price as well. We have begun additional flying in states where the state offers ICMS benefits if you fly to additional cities, so... is an example of a small city where we will start flying and that benefits not just from fuel consumption that were buy in that city but everything that we buy in the whole state. So that helps as well.

And there is a little bit of lag on between WTI and Petrobras price as well. So there is a number of small effects that account for the difference that you saw.

Mr. Amorim: clear thank you very much.

Operator: the next question comes from Savi Syth with Raymond James. Hello Ms. Syth your line is open.

Ms. Savi Syth: thank you sorry about that and thanks for the follow-up question. We have two; on the fuel hedge following up on the previous one given that you lock-in prices are you able to give some color as to what your fuel price looks like for at least 3Q and the remainder of the year?

Mr. Malfitani: most of the hedges that we have now are... Below the line, they are financial hedges. So essentially you can consider that the price of the hedge that we have is the price at the end of 2Q. That is what you are seeing here in our financials and any filtration beyond that will affect the numbers based on the mark-to-market that we did at the end of 2Q. For the next 12 months we have about 15% of our capacity hedged, which is roughly half of the maximum that we... That the policy can hedge.

If you are interested in where we built the hedging position that would be a kind of equivalent to about 205, 210 in heating oil. At the end of 2Q that all gets marked to market.

Ms. Syth: that is wonderful thank you and then if I might ask any update on the cargo JV and the timing of that?

Mr. Rodgerson: Savi we filed with the antitrust authorities about 10 days ago it seems to be progressing well. It should be a 90 to 120-day process and so we are

anxious to hear back from them. So we are still very excited about that. As you can see cargo continues to outperform even Tudo Azul and even Abhi's great revenue performance. So Abhi is a kind of lagging behind.

Ms. Syth: and then one last question on the cost side. The cost guidance given the pressure you are seeing was actually quite impressive and I was just wondering I know this year was supposed to be still a high training cost related to pilots. Where are you finding the savings? Is it mostly driven by local currency savings? I am just curious as to where you find your savings to keep that cost guidance at such a level.

Mr. Rodgerson: Savi at the end of 1Q when we saw currency devalue and fuel go up we gathered around the senior leadership team and started an initiative called 'change the business' and so we got 44 different projects across the board our senior directors are managing to take costs of the organization and improve the operational performance.

So that is the big reason why we are feeling very confident. I think in times like this when you do have spikes in fuel you start to do new things that may be were not on the table before and so we were working aggressively at those and that is part of... we can give more detail overall on 3Q and 4Q.

Mr. Shah: like we talked about a lot of it is the ramp up of the Neo capacity and the change of the business initiative that John mentioned and I think once fuel accounts for... We are talking about a 29% reduction in CASK from the Neo, I mean that is so much efficiency both from the fact that it burns a lot less fuel; but one thing that is unique about Azul, other companies will go through a change in the fleet; they are going to go from old generation jets two new generation jets but they are only going to get the fuel benefit.

We are getting the fuel benefit and we are getting the upgauging, because we built a network over time that was actually asking for this size of an aircraft. We could not have started Azul with large narrow bodies 10 years ago; but now we have built a network that has enough feed and enough traffic that can fill Neos and so we are going to get the double benefit of improved fuel burn and more economies of scale.

Mr. Rodgerson: as David mentioned the miracle of Azul was to build what we built with the aircraft we had; so now that new generation E2s are coming out, the A320neos, there is so much leverage on the business because of the aircraft we had previously.

Ms. Syth: that is helpful thank you.

Operator: the next question comes from Natalia Seraphim with Citi.

Ms. Natalia Seraphim: hi thanks for taking my question. I have two quick questions from my side, the first one is can you tell us more about the potential for an upside that could come from an alliance with the postal services? And if you see any political noise delaying the confirmation of this agreement. Thank you that is my first question.

Mr. Rodgerson: I think we talked about in some previous calls there is a logistics problem in Brazil and today Azul serves 100 cities domestically. We have 78 international cities and we have 200 stores spread all throughout the country and the Brazilian post office sends quite a bit of air freight, anywhere from six to 800 million/year in air freight and we believe that our joint venture can give them a significant reduction from what they have today and have that mail fly in the belly of our aircraft.

So I think the big difference in Brazil is that today all of that mail is palletized and so it needs specific aircraft type - and that is not how it is done in Europe or the US and. So the fact that we always have some excess space in the belly of our aircraft and so if you think about we have grown our cargo business faster than we thought was possible; and you add in the partnership with the Brazilian post office and bring in that incremental revenue that they provide and the 2000... 200 physical stores and they have thousands of physical stores throughout the entire country.

So it is not like it is in the United States. You do not send packages via Amazon to your doorstep and so having physical pickup locations is key, and so the opportunity that we are looking at is to provide a huge logistics solution for the country.

And actually I want to remind everybody it is not in our guidance and this is upside to this whole case and so we are excited about the future here and I think as you are not only providing a logistics solution to the Brazilian post office; you are providing a logistics solution for many other e-commerce players in Brazil, and that is where a lot of growth in our business is coming from.

Mr. Shah: and the Correios thing is important, if it happens that is fantastic; even if it does not our network is going to provide that to our customers and people like Amazon and others that was... other people that need logistics and Brazil is logistically challenged and no one is in a better position to help that than Azul.

Ms. Seraphim: thanks and my second question...

Mr. Shah: go ahead...

I think she said it within here; what was your second question?

Ms. Seraphim: ok sorry. My last question is quicker: do you have any comment about the Norwegian air shuttle launch in Brazil?

Mr. Shah: Norwegian looks like it is just going to fly from London to Brazil. It is not surprising, they fly to Buenos Aires, they fly to Singapore, they fly to New York. So it is not really surprising. It does not really affect us that much in any way. It is an international route for them and that is it.

Ms. Seraphim: okay perfect thanks for taking my question.

Mr. Shah: we have a question on the webcast I will just read it out here. So the question is regarding the joint venture and the progress on that. Of course yesterday Copa announced that they are in talks with United and Avianca on a Latin American - US joint venture. I cannot comment on their joint venture; but regarding with Azul and United as we said before now that Open Skies is signed we are absolutely talking towards a US - Brazil joint venture. These things take time to negotiate, we are in the process and it takes even longer to get approved actually, and it looks like the BOT right now has it pretty full docked.

But nevertheless there are opportunities for the customer for our joint business. So we are actively talking to them regarding a US - Brazil joint venture with Azul and United.

Mr. Rodgeron: and this was always in the plans. When United made their investment in Azul before Open Skies was approved we knew that this was a possibility and so we kind of wrote that in a contract that we have with them and United has been a fantastic partner of ours and we love the fact that they bought a portion of the HNA shares a few months ago, which shows their confidence in our business as we move forward and shows the upside that they believe in Azul.

Operator: Excuse me. As a reminder if you would like to pose a question please press star one.

Ladies and gentlemen this concludes today's question-and-answer session. I would like to invite John to proceed with his closing statements. Please go ahead sir.

Mr. Rodgeron: I would like to thank everybody for joining us today and as always if you have any follow-up questions we are available. We will be doing calls all afternoon and certainly call up Andre and we are glad to deliver on our plans. Thanks everybody, see you next quarter.

Operator: That does conclude Azul's audio conference for today. Thank you very much for your participation and have a good day.

