

Transcript of Avianca Group International Limited First Quarter 2024 Performance Call

April 30, 2024

Operator

Good morning, everyone and welcome to Avianca Group's Q1 2024 Performance Call. At this time, all participants are in a listen-only mode, and we will open the floor for questions after the presentation. [Operator Instructions] Please note, this conference is being recorded.

I will now turn the conference over to your host, Maria Ricardo, Head of Investor Relations. Maria, you may begin.

Maria Ricardo - Head, Investor Relations, Avianca Group International Limited

Good morning, everyone and thank you for joining us today. With me today are; Adrian Neuhauser, Chief Executive Officer of Abra Group; Frederico Pedreira, Avianca's Chief Executive Officer; Rohit Philip, our Chief Financial Officer; Gabriel Oliva, Avianca's Chief Operating Officer and Avianca Cargo Chief Executive Officer; and Matt Vincett, LifeMiles' CEO.

Financial statements for the period ended March 31st, 2024 and the presentation that we will show you today are available at our investor site. Today's conference call is being broadcast and a replay will be available at the same site shortly after the end of the call.

Before we proceed, I would like to remind you that during this call, management will make statements or remarks that may be forward-looking statements that may include, but are not limited to, financial projections or other statements of the company's plans, objectives, expectations or intentions. These matters involve certain risks and uncertainties that could cause actual results to differ materially from those projected or suggested.

Today, Fred will start our call with an overview of the state of the business and then Rohit will walk you through our first quarter 2024 financial performance. As always, our prepared comments will be followed by a question-and-answer session.

With that, let me turn the call over to Fred.

Frederico Pedreira - Chief Executive Officer, Avianca Group International Limited

Thank you very much, Maria. Good morning, everyone and welcome to Avianca's first quarter 2024 performance conference call. As Maria mentioned, I'll kick off with a couple of highlights from the first quarter. So we continue to deliver strong results in a quarter that is not one of the strongest of the year and that can be seen with an EBITDAR of \$272 million in the first quarter, representing a 21.5% margin. Our net income for Q1 was \$30 million.

Our passenger CASK ex-fuel was 4.1%, that aligned with our guidance that Rohit gave in the previous call and impacted by the Colombian peso versus the United States dollar. On the CASK, I also want to mention that we continue to see a positive CASK trend despite the pressure on the Colombian peso.

We end up the quarter with \$971 million and our net debt to last 12 months EBITDAR was 3.2 times. LifeMiles continued with the strong value creation, when, in particular with a cash EBITDA contribution of \$36 million in the quarter, which is a 15.3% increase compared to Q1 '23. Avianca Cargo revenues were at \$152 million, which represents an 8.3% year-on-year decrease and where the key variables here has been the overcapacity in the markets. As you know, one of our main competitors has increased a lot their cargo capacity in the market.

However, we continue ahead of our business plan and important to mention, starting Q3, we expect a significant improvement in efficiency from an operational and cost 10 points as we will start the process of re-fleeting our old A300 and 767 cargo fleets to the new 330F that will start delivered in June. June 15 will be the first.

Couple of other milestones worth mentioning before passing on to Rohit. We resume the Bogota-Caracas route and we announced a couple of new routes, that the most important ones I will just pick up a few Bogota-Montreal, Bogota-Paris starting on July 3rd, Medellin-Buenos Aires and Medellin-Santiago and Medellin-Lima.

We've also recently opened the sales for our Business Class service on the narrowbody that will start operation in July 1st and will offer 11 destinations out of Bogota. That decision was driven by the good performance that we've seen since we re-launched our Business Class in the Americas in the widebody.

Last but not the least, our first reconfigured 787 started operations last week. This is the first one now operating with 291 seats, which is a 16.4% increase compared to our former cabin. And we're on track to receive the second one in two weeks. And the plan is to have 13 787s fully densified by the end of the year.

Moving on to operational performance. Our on-time performance in Q1 was of 85% and our scheduled completion of 99.1%. This is a very good performance if you consider the growth in passengers for queue, and in particular, the added pressure on Bogota.

So in last December, Bogota increased their operations per hour from 66 to 74. That was a concern that we had in terms of if the airport would manage this additional capacity well. And working with the authorities and our partners, we have been able to, in spite of that significant movement growth in Bogota to maintain a topnotch on-time performance and schedule completion.

Last, but not the least, and I can say that without hesitating, we continue with a world-class mishandled baggage number at 1.3 in the first quarter when, according to CEDA, the average in the world is above 7.

And with that, I'll just pass to Rohit.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Thank you, Fred and good morning, everyone. Moving to Slide 4 and unit revenue, our Prask for Q1 was \$6.7 cents, a 3.1% reduction compared to last year on a capacity increase of 26%. You can see load factors were up 1.2 points at 81.4% with yield slightly down to \$8.2 cents, 4.5% lower than last year. So overall, with this large capacity increase, we're quite pleased with the revenue performance in the first quarter.

If you go to Slide 5 and look at unit cost metrics, you can see our passenger CASK ex-fuel was \$4.1 cents for the quarter, which was in line with guidance when you adjust for the strengthening of the Colombian peso, which as a reminder, affects our cost and revenues about equally. So we are margin neutral on the peso, but it affects our costs. And this \$4.1 cents is aligned with the guidance we gave.

Fuel CASK was down year-over-year by 15%. So you can see total CASK was \$6.2 cents compared to \$6.4 cents a year ago. And importantly, when you look at our cost structure and look at it compared to 2019, where total CASK was \$7.1 cents, you can see why we can make money at the same fair levels that we could not make money in 2019. So this is really an important proof point of the new business model.

Moving to Slide 6 and talking about cargo performance, as Fred mentioned, cargo revenues were down 8.3% year-over-year, but importantly, still ahead of business plan. If you recall, in the business plan, we always projected that the cargo demand that we were seeing in the pandemic would start to moderate. And so you can see that obviously that has happened. And while it's slightly down year-over-year, it's still ahead of our business plan projections.

And as Fred said, we are going through a re-fleeting process. So if you recall, our cargo business has 11 aircrafts, six A330 freighters in our Colombian operation and five older aircraft in our Mexican operation. And the five older aircrafts, the B767s and A300s will be replaced, as Fred mentioned, by three A330 freighters over the course of the next year. And that will bring significant efficiencies to the freighter business and that's what we'll see going forward.

Moving to Slide 7 and LifeMiles. LifeMiles, we saw strong performance in the quarter with third-party gross billings at \$59 million, significantly ahead year-over-year, and importantly,

at slightly higher than the levels we saw pre-pandemic. And cash EBITDA was strong at \$36 million for the quarter.

With that, moving to Slide 8. Overall, we generated EBITDAR of \$272 million at a 21.5% margin, a 16% increase year-over-year, and net income at positive \$13 million. Moving to Slide 9 in cash flow, you can see we ended the quarter at \$971 million.

And it's important to sort of walk through some of the elements of cash flow for the quarter. Obviously, starting with the \$272 million of EBITDAR, we had corporate debt, lease payments and CapEx that were largely in line with the guidance I had given for the year for these three categories.

And then working capital, there are a couple sort of items that I'd like to explain. In the fourth quarter, we had explained that we had a timing benefit of \$33 million of payments – that of December payments that were ended up made in January. So that reversed obviously in the quarter.

And in addition, we actually had a timing issue in working – or timing impact in working capital with respect to the last week of March, which was Holy Week in most of our markets, where we had sort of two impacts, some receivables were collected in the first week of April.

And so the last week of March, a lot of the settlements came in April. And then we have to make some of our lease payments for April in the last week of March, because the payment date was a holiday. And so you'll see that that will reverse in April. So that was the impact on working capital.

The other impact in working capital is ATL. So the first quarter, which is our Advanced Ticket Liability for forward sales in the first quarter, typically you'll see sort of a lower ATL build because Q2, especially April and May tend to be low season, and in particular, April, while last year we had Holy Week in April, this year Holy Week wasn't in April.

So you see sort of a lower build of ATL that combined with, we do see sort of a return to more seasonal – seasonality in terms of our low season and high season that we discussed also on the last quarter call.

And as a result, we do see a little bit more of the low season impacts in April and May that would be based on the forward sales that we've seen. So that's cash. If I move to Slide 10 and talk about our balance sheet, our net debt at the end of the quarter was \$3.9 billion and our leverage ratio at 3.2 times that was healthy balance sheet.

With that, I will turn the call back to the operator to start our Q&A.

Operator

Thank you very much. We are now opening the floor for questions. [Operator Instructions] Thank you. Your first question is coming from Neil Glynn of AIR Control Tower. Neil, your line is live.

Q: Good morning, everybody. If I could touch on two themes, please. The first one with respect to unit costs, I wondered if you could confirm what the constant currency ex-fuel unit cost development year-on-year whilst to strip out that Colombian peso impact. I realize it's a wash at the operating level.

And tied to that, the personnel costs were up about 40 – I think it was 44% year-on-year. If you could help us understand what's the underlying currency adjusted development there that would be helpful. And then the second question, you said again today, as you did at the full year, that normal seasonality is resuming. So I'd be interested to get your take on how the second quarter margin should evolve.

If you look back, pre-pandemic, I appreciate the cost base is very different, but we had seen quite some volatility side. So we'd seen 19% in 2017 in the second quarter. We'd seen 14% in the second quarter of 2018. And then obviously 2019 was very weak. So just interested on how you would manage expectations around that margin. Thank you.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Okay, thanks. Hi, Glynn. Thanks for the questions. So, starting with your question on CASK ex-fuel and the currency impact, so the way – we guided our CASK for the year at \$3.8 cents to \$4 cents. So the midpoint of that range would be \$3.9 cents.

And with the currency impact, which we gave sort of the adjustment, sensitivity adjustment on the last call, if you use the math that we gave last time, you'd get a number of \$4.03 cents. Our number was actually \$4.07 cents, so that rounds to \$4.1 cents. So that's the currency impact. So it's largely aligned with year-over-year – it's largely aligned with guidance and pretty much year-over-year – when you adjust for the currency.

Fred?

Frederico Pedreira - Chief Executive Officer, Avianca Group International Limited

No, just also mentioning that at the end of this year, December to January, for frontline workers, we also did something in terms of our labor cost that is worth mentioning, which is a lot of those frontline workers haven't been adjusted fully by inflation since 2019.

And these are basically the workers with the lowest salaries. So we decided to, for all our frontline workers, give basically inflation from 2019, cumulative inflation from '19 to '23. So that effect was a one-time hit that we thought it was essential to ensure the wellbeing of all our labor force.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

And just to add to that, on labor, on the overall increase, there's basically three impacts, including the one that Fred just talked about. So first is the currency impact on labor, which is about 15% year-over-year. So that's the first part. The second is the increases that Fred mentioned that we caught up on sort of the inflation adjusted increases over the last three years in the second half of last year. So you see that impact in the year-over-year numbers.

And then the third is our capacity was up – 26% year-over-year. So there is more frontline employees, even though we've improved productivity significantly. But if you add the impact of the three that explains more than the increase offset by obviously the productivity increase.

Now, the third question you had, Neil, was on 2Q seasonality. And on 2Q seasonality, we do see we'll have a little bit more of moderation in April and May, followed by sort of a stronger June and the third quarter based on sort of the forward bookings that we see. In terms of specific margin guidance, we're not in the position to really give that, but directionally that's what we would expect.

Q: Thank you.

Operator

Thank you very much. Your next question is coming from Chris Reddy of BNP Paribas. Chris, your line is live.

Q: Hey, good morning, guys. Thanks for taking time for the call. Very good results once again. Could you just refresh my memory on the cadence of deliveries for the rest of the year? And what sort of percent increase in capacity that represents?

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Sure. At this point, we do not have any additional sort of narrowbody deliveries. Sorry. So, we have our order book with Airbus starts to deliver in 2025. For this year, we have five additional aircraft deliveries that were in – that we had incorporated into the guidance both for capacity and for our fixed costs in terms of lease rentals for this year.

So we have five more deliveries that are coming through the course of the year that those deliveries tend to be later than what we expect because of deliveries – delays in sort of the Airbus delivery stream. But we do have five additional aircraft coming in and then we've got these three 787s that are not flying today. So, just important to note, we have – 16 787s on our books, only 13 of which are flying.

Actually only 12 of which were flying, because one of them has been sort of in the densification line for – had been densified but had been waiting on sort of all the regulatory

approvals on the new configuration, and so was on the ground for a while. Now that we've gotten the approval, now, as Fred mentioned, with the rest of the densification line will get done for the other 13.

So out of the first 13, one of them has been not flying. And then of the three additional 787s that we're still in the process of incorporating, two of them will fly later this year. And that'll add the additional capacity. So those are the capacity changes.

Q: Okay, great. Appreciate it. Thanks again for your time.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Thank you.

Operator

Thank you very much. Your next question is coming from Ian Snyder of J.P. Morgan. Ian, your line is live.

Q: Great, thanks. And congratulations on the results, team. Last quarter on the earnings call you noted that you're exploring alternative options for the LifeMiles loan given the cost of capital is over 10%, and you think that there's a more efficient way to utilize the associated collateral? Can you give us an update on any of these options that you're looking for? And then any comments on LME or liability management for the bonds itself as well?

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Sure. Hi, Ian. As far as LifeMiles are concerned, that was sort of a little bit more of a conceptual conversation. I think we're not looking at sort of actions on that. We're quite satisfied with the current structure of it. The only thing is, as the loan amortizes, it's not the most efficient use of the collateral.

So, in the short-term, maybe it's just similar structure, but just re-levering that collateral. But over time, there are more options that we've been studying, but that's not immediate term. In terms of the bonds, again, no current sort of expectation to make any changes on the bond – on our bond.

Q: Great. Thanks a lot for the time. I appreciate the answer. That's it for me.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Thanks, Ian.

Operator

Thank you. [Operator Instructions] Our next question is coming from Michael Kaufman of Redwood Capital. Michael, your line is live.

Q: Thank you. Thank you for the call – taking financial questions. Can you discuss that on the Prask decline this quarter, can you give us a little bit more information on how you see that going through or going evolving over time? Is this driven by some mix shift versus incremental capacity year-over-year or market weakness or how do you anticipate that performance over time?

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Michael, we didn't get the full question. Can you just repeat the question again?

Q: Sorry about that. I was wondering if you could discuss the drivers of the Prask decline this quarter and how you see that evolving over time. And is it just, we need to make sure some of the routes. Is it mix shift? What do you think is happening there?

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Yeah, sure. Let me start and then let Fred and Adrian jump in as well. So firstly, as you know, we increased capacity significantly in the – on a year-over-year basis. Obviously, that capacity increase was put in – took place in the fourth quarter. We're very pleased with how the capacity has been absorbed into the market, but it is a significant capacity increase and you would always expect a little bit of yield decline when you add capacity. So that's sort of point one.

Point two on – with respect to the capacity deployment. There are regions that we've talked about that have some weakness. We've mentioned in the past that there's been a lot of pricing activity in the Central America to North America market, where [inaudible] in particular has been very aggressive with very low fares. And so you see a little bit of an impact year-over-year in that particular market, which was very strong a year ago. So I would say those are the two things I'd point out. Adrian, you want to add anything?

Adrian Neuhauser - Chief Executive Officer, Abra Group Limited

Yeah, Mike, hey it's Adrian. Let me chime in for a sec. Just so to give you a little bit of perspective of how we look at it, right. And part of how we look at it and as we continue to expand our network, part of how we look at it is, this is sort of the nature of what we're doing, right. We're going to have skirmishes here and there as we either protect market share or grow.

And so, as Rohit said, right, Central America and North America is basically, Prask has been impacted pretty significantly, whereas that was a very important source of profitability a year ago. In this quarter, we're seeing a little bit more activity in domestic Colombia. But ultimately, this is why we are as focused as we are on having better costs than our competitors is because this is going to continue to happen.

You're going to continue to see shift as people test where we have strengths or pushback on our market share captures or what have you. And so you'll sort of see the battleground move, right. And our focus is to continue to be profitable and to continue to be cost competitive as we sort of fight these battles that are inevitable, right. As Fred – he'd already mentioned, right, you're seeing a big pullback of US carriers from Latin America, right. We think we are largely the cause of that and we're proud of it, right.

Ultimately, this is, as we become more cost competitive and we can tolerate lower Prasks, while still being profitable, it makes it more difficult for carriers that have structurally higher cost to compete and remain in the market. And over time, that will become recover margins as well in a structurally healthy fashion.

So we're happy to give you details, but I guess the punch line is, from where we sit, this is just sort of business as usual. And you'll see kind of the battlegrounds shift and move and one quarter it'll be one place, next quarter it'll be a second. But we think that as long as we continue to be the network carrier with the cost leaning structure in our market, we're going to [inaudible].

Frederico Pedreira - Chief Executive Officer, Avianca Group International Limited

I would just add one more thing, which is, if you look at our fourth quarter yield performance year-on-year, you'll see a significant drop that's when we increase the big bulk of our capacity. But if you look at Q1 year-over-year our yield drop, you'll see that is significantly low, less than half the yield drop that we saw in the first quarter.

That tells us, and that the capacity is being well received by the market. And, of course, we will have, as Rohit mentioned, this year we'll have a low season that we didn't have last year, right. But overall, the trend – we've seen a positive trend in the yield.

Q: Great. Thank you for that color. Appreciate it. Two other quick questions for me is, can you remind us what the guidance was full year for CapEx and all-in aircraft expenditures, so lease plus financial leases plus PBH?

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Yeah, we had guided \$1.1 billion for the full year. It's on the slide in the Q4 presentation for the combination of net payments, lease payments and CapEx.

Q: I see. And – I'll go back and look at that. Can you give us a specific CapEx number or could you comment on whether this CapEx this quarter was a little bit heavier or lighter than you would expect?

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

It's in line with what we'd expected. I think if you look at the combination and you can reconcile this with me and Maria Cristina offline, but if you look at basically the combination

of the three, it's in line with the full year guidance with the exception that debt payments obviously are a little bit lumpy in 2Q and 4Q, because of the indenture payment is in 2Q and 4Q. So if you adjust for that, you'll see that this is right in line with guidance, but happy to reconcile it offline.

Q: Great. Thank you. And then one last one. In terms of seasonality, when you think through the quarters, now that we're kind of back to a normal seasonal cadence, can you just remind us quarterly what you think the order of – just like the order of the quarters would be? So one is, would 1Q be weaker than 2Q and then 3Q and 4Q kind of roughly comparable, but better than 1Q and 2Q? Is that the way to think about it?

Frederico Pedreira - Chief Executive Officer, Avianca Group International Limited

Yes, that's very – so Q2 is the weakest quarter, from the weakest to the stronger. So Q2 the weakest, then Q1, right, and then the second half of the year is always better than the first half. So, in the second half of the year, you have from end of June to August that is high season, and then end of year December, which is also very strong.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Yeah. So Q3 and Q4 tend to be, some years Q4 is stronger, some years Q3 is stronger, but Q1 is usually better than Q2, because in Q1 you have the January effect as well, where you have some of the high season, especially the southern cone has that summer still going through and we get a little benefit of that, not as much as like a LaTAm would or our Brazilian carrier would, but we get a little bit of that. So, it's really Q2 versus Q1 and then Q3, Q4.

Frederico Pedreira - Chief Executive Officer, Avianca Group International Limited

And just one other small info, which is between Q1 and Q2, where there's the Holy Week sometimes impact. So it depends on if it's in Q1 or Q2 can change a little bit the dynamic, but it's, again, overall, Q1 is stronger than Q2.

Q: Great. If I could flip one last one, and you mentioned 3 of the 787s you're still densifying. Are there any other planes that are getting densified? Or are we basically through that at this point?

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

No, sorry. I think you misunderstood. So all the 13 787s that we have currently flying are in the process of being densified and will be densified in the next year. So the additional three that we have put already on our books are not yet flying. And so, those are the ones that will enter into service into our operation over the course of this year. Two of them will enter in the course of this year, and the third one will be early next year.

So those are – but they will all be densified eventually. Just a reminder, the current 787s in the Avianca configuration at 250 seats, 28 business and 222 at the back. The reconfigured

cabin will have 20 business class – 20 lie-flat business class seats. So eight less business class seats, but 270 at the back or 271 at the back. So it's a total of 291 versus 250, which is a significant improvement of the efficiency of real estate in the cabin.

Q: Great. Thank you very much, team. I appreciate it.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Thank you.

Operator

Thank you very much. And your next question is coming from Robert Green of FourSixThree Capital. Robert, your line is live.

Q: Hi. Thanks for taking the call. I just want to expand on one of the points from the prior question, which is, so if Q2 is expected to be seasonally weak or so – weaker than Q1, should we then be expecting EBITDAR to be down year-over-year for Q2? And by extension, how should we roll that out in terms of expectations of net leverage reduction over the full course of the year? Thank you.

Rohit Philip - Chief Financial Officer, Avianca Group International Limited

Again. I think we'll stay away from giving specific sort of guidance on EBITDA for Q2, but I think just directionally, you'll see sort of lower margins in Q2 versus Q1, and then much higher margins in Q3 and Q4. That's just directionally how we'd go again in terms of net leverage, it will depend on EBITDA performance, which right now, we're not being able to – we're not in a position to guide, but we would continue to strive to deliver the de-levering that we've been delivering over the last couple of years.

Operator

Okay, thank you very much. That appears to be the end of our questions. [Operator Instructions] We don't appear to have anyone else in the queue. I will now hand back over to Fred for any closing remarks.

Frederico Pedreira - Chief Executive Officer, Avianca Group International Limited

Thank you very much, everyone for being with us today. And before closing this call, I would like to express my gratitude to an amazing team of Avianca employees that work hard every day and have contributed to the success that you have seen in the first quarter.

And I would also like to thank our investors, customers, partners that for all their support. As we move forward, we will remain focused on executing our business plan and our transformation. And we look forward to meeting you in a quarter from now for the Q2 results. Thank you, everyone.

Operator

Thank you very much, everyone. This does conclude today's conference. You may disconnect your phone lines at this time and have a wonderful day. Thank you for your participation.

About Avianca Group

AVIANCA includes Avianca – a Star Alliance member-, LifeMiles and Avianca Cargo. In passenger transportation, Avianca, with more than 103 years of continuous operation since 1919, is the leading airline in Colombia, Ecuador, Central America and has one of the largest air operations in Latin America with more than 145 routes, 3,800 weekly flights and a passenger fleet of 147 Airbus 320 and Boeing 787 Dreamliner aircraft, connecting to 76 destinations in 25 countries in the Americas and Europe. In 2023, Avianca carried 31.9 million passengers with the operation of more than 187,000 flights. Its loyalty program, LifeMiles, is one of the largest in Latin America with more than 12 million members and 400 allied brands. In cargo transportation, Avianca Cargo is a leader in the region, serving more than 53 destinations with a fleet of Airbus 330 freighters, in addition to operating bellies in passenger aircraft. In 2023, Avianca Cargo transported more than 500,000 tons of cargo. Avianca today has a team of more than 13,000 people committed to providing safe, convenient, affordable and friendly service to its customers. More information at www.avianca.com