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# EDITED TRANSCRIPT

LAN.SN - Q4 2014 Latam Airlines Group SA Earnings Call

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## PRESENTATION

### Operator

Good day, everyone, and welcome to the LATAM Airlines Group earnings release conference call. Just a reminder this conference is being recorded.

LATAM Airlines Group earnings release for the period was distributed on Tuesday, March 17. If you have not received it, you can find it on our website, [www.LATAMAirlinesGroup.net](http://www.LATAMAirlinesGroup.net), in the investor relations sections.

At this time, I would like to point out that statements regarding the Company's business outlook and anticipated financial and operating results constitute forward-looking comments. These expectations are highly dependent on the economy, the airline industry, and international markets; therefore, they are subject to change.

Now it is my pleasure to turn the call over to Ms. Gisela Escobar, Corporate Controller, IR Officer of LATAM Airlines Group. Please begin.

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### **Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Thanks very much. Good morning, everyone, and thanks very much for joining our call. We're going to go over today our financial results for the fourth quarter of 2014 and the full-year 2014.

If you look at the slide presentation that's available on our website, going to the first slide we just wanted to give some highlights of the most important events that occurred during 2014 for LATAM Airlines Group.

The first couple of points refer to the restructuring that we have been doing on our balance sheet. This is something that has been ongoing for the past two years. And one of the main objectives here has been to reduce the exposure on the TAM balance sheet to the Brazilian real that has allowed us to mitigate the effect in terms of the exchange rate differences that we see in our P&L that results from the devaluation of the Brazilian currency.



We have consistently reduced that. The exposure on the TAM balance sheet was \$4 billion in 2012 and has come down to approximately \$600 million at -- as of the fourth quarter of last year.

We have also continued to do the restructuring of our fleet plan. We have significantly restructured our fleet plan over the past couple of years. That continued during 2014.

Over the last 12 months we have reduced our fleet commitments for the period between 2016 and 2018 by \$1.8 billion, basically by reordering and postponing and changing certain of our aircraft deliveries that were scheduled, in order to have a fleet plan that adequately meets our growth needs.

Also relevant during 2014, we have continued to receive the new technologies of wide-body aircraft. We received five additional 787-8s. With that, we ended 2014 with a total of 10 787-8s in our fleet and we expect to end this year with 17 of those aircraft, including the 787-9s which we will be taking delivery of this year.

Now we start seeing really that these new technologies of aircraft become of critical mass and become more representative within our wide-body fleet, which is obviously very positive from the perspective of a continuous reduction in cost per ASK as well as from the perspective of the passenger experience.

During 2014, one of the major events in Brazil was the World Cup tournament, which occurred during the months of June and July. We saw in Brazil a very successful execution of this event, which was obviously very, very significant because of the amount of travel that was concentrated in the 12 cities in Brazil where the World Cup was taking place.

So although this had a negative effect for us in terms of the impact it had on corporate demand, there was a very successful execution of the event and we are seeing today the long-term benefits that this created for the airline industry, specifically relating to airport infrastructure. And that refers to the next point.

We were able to move all of the international operations of LATAM Airlines Group to the new terminal three at Guarulhos airport. During the fourth quarter of last year we completed that move and that allows us to really consolidate Sao Paulo as the main hub for LATAM Airlines Group within South America and provide improved connection times for our passengers traveling through that hub.

Finally, it is also important to mention that TAM officially joined oneworld during 2014 and, as such, a oneworld became the global alliance for the whole of LATAM Airlines Group.

If you turn to the next slide, you can see the numbers for the fourth quarter and for the full year. The trend that we saw during the full year that was the same during the fourth quarter is basically a reduction in terms of revenues. Overall, we saw a reduction of approximately 1% in our total ASKs last year, and in addition to that we start reductions in revenue per ASK that were driven by the devaluation of corporate currencies and a challenging competitive environment in the region that we will talk about a bit later on.

But all of those things resulted in a reduction in terms of operating revenues that was 8.6% for the quarter and 6% for the full year. In the quarter, this was more than offset by a reduction on the operating costs that was over 10%. And there were different effects, but there we saw the other side of the devaluation of local currencies, which is -- for the percentage of our costs that are denominated in local currencies, a devaluation is positive for our cost performance.

And we also saw the decline in fuel prices last year, which obviously helped us on the cost side, in addition to the benefit that we are seeing from a lower cost per ASK as a result of our new fleet.

With that, our operating income for the fourth quarter reached 8.6% and for the year we were in line with the guidance that we had already provided with the operating margin of 4.1%. On the net income side, we had net income in the quarter of \$98 million and for the full year a loss of \$110 million.

If you go to slide 4, this just shows you graphically, more or less, the numbers that we were seeing on the previous page, but here you can see very clearly that the strong improvement in our margins this quarter comes from a cost performance. When we look at revenue per ASK, we had a decline in revenue per ASK that was driven by lower yields and not lower load factors, so load factors were up on average for our whole operation by 1.3 points. But our yield was down.

And then we had the positive impact of fuel, which was significant, and then other costs including wages and benefits and other costs lines, which also impacted positively our operating margins.

On the next slide, turning to page 5, you can see the breakdown in terms of the decline in our total revenues per ASK. If we look at the main contributors to this \$0.076 revenue per ASK and the 12.5% decline there, basically what we saw in the international passenger business was that we had capacity relatively flat during the fourth quarter, an improvement in load factors that was driven by a 1% improve -- increase in traffic as measured in our PKs, and a decline in revenue per ASK of approximately 7% that came mainly due to lower yields.

Those yields were basically driven by what we had been talking about and the same trends that we already been seeing during the first three quarters of the year, which had to do with mainly a very challenging competitive environment in the region, with a lot -- most international players significantly adding capacity to South America on the routes where we are flying.

When you look at the domestic Brazil operations, we have overall a revenue per ASK decline of 13.5%. This number, if we look at it in Brazilian currency, is approximately 6% and is higher basically as a result of the devaluation of the Brazilian currency. Here also we had an improvement in load factor of approximately 2 points, so capacity was up 2.7%. Traffic was up significantly more than that and load factors were very healthy at 83%.

And on the Spanish-speaking countries, which represent 17% of our total passenger capacity and which include our domestic operations in Chile, Argentina, Peru, Ecuador, and Colombia, there we are growing capacity at approximately 5.5%. Traffic, again, increasing more than that with load factors increasing by 1 percentage point. And with that revenues per ASK were down by 6.6%.

That 6% decline is mainly driven by the devaluations that we were seeing in the local currencies and that we saw during the fourth quarter in the different local currencies. The Chilean peso during the quarter devalued by 15%. The Peruvian currency devalued by 4%. The Argentine peso devalued by 39%, so obviously all of those devaluations affect the domestic yield.

If we go to the next slide just to talk a little bit about cargo, in cargo we continued to see a fairly weak market trend. There is an overcapacity in the region with a very challenging competitive environment and we see that demand, especially important demand into the region, has not really seen a recovery.

So here our focus continues to be very much on managing our capacity between bellies and freighters. We are focused on making the maximum utilization of our belly capacity and on adjusting our freighter capacity in order that it serves to support the belly operation. But we are looking for opportunities to further reduce our freighter capacity, given the context that we are in.

The good news here is that we finalized last year the sublease of three 767 freighters to another carrier that operates outside of the region, so two of these freighters already are not in our fleet as of December of 2014 and we have one more these freighters that will be subleased during the first quarter of 2015. This allows us to continue to adjust our capacity to the current challenging environment in cargo.

We just wanted to mention briefly our exposure to the main macro variables. Obviously we have seen a significant amount of volatility during the first quarter and especially during the past few weeks, both on the fuel side and in terms of the currencies. When we look at our exposure to the Brazilian real, we have a larger percentage of our revenues than of our costs denominated in real.

So we have overall as LATAM approximately 30% of our total revenues denominated in Brazilian reals. That comes mostly from the domestic operation in Brazil and we have approximately 25% -- 24% of our total costs denominated in reals. This translates into an operating exposure of

approximately \$750 million per year to the real. And of that we have hedged up to today \$375 million of those approximately \$750 million at an average rate of approximately BRL2.8.

This obviously does not include the impacts that a devalued real could have in terms of demand in the Brazilian market. This is just the exposure in terms of the mismatch, in terms of our revenues, and of our cost.

When we look at fuel, our current fuel hedge position is approximately 30% of our estimated consumption for the full year with the breakdown that you can see in the graph on the bottom right-hand corner. For the first quarter, we are hedged approximately 30% of our consumption.

At the prices that we have taken, these hedge -- our current estimate is that we would have a negative impact of approximately \$200 million, \$215 million for the full year as a result of these hedge positions. At current fuel prices, obviously the benefit from the significant decline that we've seen in fuel prices over the past weeks obviously much more than offset this loss.

When we look at this year, we have not changed the guidance that we had already provided in January for our results for 2015. We are expecting currently to grow in terms of total passenger capacity by between 2% and 4% with a somewhat higher growth on international routes, between 4% and 5%, and a somewhat higher growth in the Spanish-speaking markets between 4% and 5% as well. In domestic Brazil operations, we are expected to remain flat in terms of capacity growth.

And on the cargo side, we have a small growth in terms of capacity that is mostly coming from the increase in the belly capacity from the long-haul passenger operations. So we don't have any additional freighters; on the contrary, we are reducing our freighter capacity.

With that, we expect to have a significant increase in terms of operating margins this year. Our current target is 6% to 8% operating margins for 2015.

In -- we've talked a little bit about the main focuses that we have for 2015. In terms of our strategic plan that we are implementing, there's three important critical success factors that we are focused on. The first one has to do with the network, which basically is focusing on increasing capacity on routes that have a higher yield and on really consolidating our hub strategy throughout the region.

We continue within domestic Brazil to be very disciplined in terms of capacity and when we look at our international growth, our growth is very much focused on certain specific opportunities. And beyond that basically comes only from flying the same routes with larger aircraft. So it is a very low-risk growth in the sense that we are basically putting larger aircraft on the same route and flying that same route with a lower cost per ASK.

We also are looking more strategically in terms of our network to really leverage the leadership position that we have in the region and the connectivity that we have in the region, which is, by far, the best compared to all of our competitors because of the presence that we have in seven different countries throughout the region. And because of our leadership position in most of those countries.

In terms of customer experience, which is another very important -- a critical factor that we are focusing on, we are focusing on improving our product and improving our passenger experience and we're going to talk a little bit more about that. In terms of cost, we've already mentioned we have a target of \$650 million run rate in terms of cost reduction to be achieved over the next three years. This is net of one-time costs, so we already expect to have in the guidance that we have provided a reduction in terms of cost per ASK coming from these initiatives, which are already in place since the end of last year.

And in addition to the \$650 million of these efficiencies, we are also advancing with the fleet plan and the new fleet comes with a lower cost per ASK. So the \$650 million that we have mentioned is in addition to the cost per ASK reduction that we are going to see as a result of a more efficient fleet.

When we look at our domestic Brazil operations in our networks in Brazil, our focus for this year is on consolidating our hub in Brasilia -- our hub strategy in Brazil with our hub in Sao Paulo and a hub in Brasilia. Brasilia is an airport that, as we already mentioned in the past, is a new airport. TAM recently moved its operations to pier two at Brasilia airport, which the picture of the slide shows the Brasilia airport.

Brasilia is a very attractive place to build a hub because of its very good geographical location. It's much more central within Brazil, and also it is, obviously, the third-largest market in Brazil and has a higher GDP per capita relative to basically most other cities in South America.

We have a strong competitive position in that city and we have plans to add 11 destinations in total from Brasilia during this year. That will allow us to increase significantly the number of city pairs that we serve through Brasilia, and so this is going to -- the growth in Brasilia is going to offset reductions in some of the other routes that we are having, where also, as we have mentioned before, we are seeing a negative impact from the declines in corporate demand. So the growth in Brasilia is consistent with the 0% or flat capacity growth that we have during the year because it is offset by declines in other parts of our network.

The other important thing to mention in the domestic Brazil operation, which we have already also talked about in the past, has to do with our regional strategy. We are increasing. We are planning to serve between four and six additional regional destinations per year in Brazil. These are smaller cities; cities that have basically between 100,000 and 1 million passengers. And we are starting to operate those cities, at least in the short term, with an existing current fleet that we have, which are the A319 aircraft.

When we talk a little bit about our international passenger operations, here we are talking about in our long-haul and regional operations we have basically two important things to mention. As we already talked about, we are growing on these routes approximately 5% in terms of ASKs.

This growth is very much focused on routes that we already serve, but that we are planning to expand operations on with more efficient aircraft. And also very specifically expanding our Caribbean operations with additional frequencies that we have added and new routes that we have started to certain more tourist destinations in the Caribbean.

The other important part of the strategy for our international operations has to do with the product enhancement and with the fleet, which basically is more relevant this year because we are seeing an increasing number of aircraft with new technologies in our fleet. So we are going to end this year with 17 787s in our fleet, which are 12% more efficient to operate than the 767s. And also towards the end of the year we are receiving our first A350, which is also more than 20% more efficient than the A330s that we currently operate.

The other important thing I would mention here is that we are also not taking anymore deliveries of 787-8s. All of the 787s that we are receiving now going forward are the 787-9s, which, because they are larger, are 13% more efficient than the 787-8.

In terms of the customer experience, we are focusing here on basically improving and transforming the passengers' customer experience on different fronts. First, we are making changes in terms of the experience on the plane, so we have been already for the past years working on a single-cabin field for both the LAN and the TAM fleet. We already have this implemented on our first 787-9 and on our A321.

We are -- that is in terms of just the onboard experience. We are also incorporating a TAM with the retrofit of the 777 fleet. We are phasing out the first class and incorporating the premium business class, so that's a more similar experience between the LAN and the TAM flights. And we are changing a little bit the onboard service to make it also a more harmonized experience between the two airlines.

We have new VIP lounges in many of the cities that we operate. Obviously at terminal three at Guarulhos is our largest and newest VIP lounge, and we will be opening very shortly in Santiago a new VIP lounge as well.

Our new customer experience basically focuses on a much more mobile experience, where we not only want to make the passenger experience better during the flight, but we also want to be able to have passengers to manage better their time and to manage better their own passenger experience. So we have different examples -- a very important part of the passenger experience is the digital strategy.



We have different examples here on slide number 14; some in terms of apps, in terms of what we are doing to allow passengers to remain connected during the flight. To be able -- we are the first airline in the region that allows the use of mobile devices during the flight, although still in airplane mode. And we are working on a wireless in-flight entertainment system on our narrowbody fleet.

If we go to the next slide, another important point to mention is that we are -- have a very strong performance in all of -- throughout our network in terms of on-time performance. Here we are measuring on-time performance with a 15-minute standard. In our Spanish-speaking countries on-time performance is close to 87%. It's approximately 84% in domestic Brazil operations and 82% in international operations overall. In all cases, an improvement over what we had last year.

And, finally, just a brief comment in terms of our fleet plan. This is something that has not changed, but we are expecting to invest in terms of fleet commitments this year approximately \$1.7 billion. This is partly financed with debt and partly financed with sale and leasebacks, so it's not -- all this \$1.7 billion is not debt that is going on the balance sheet, but it is a total dollar amount of the aircraft that we are delivering this year.

Despite that, if you look at the graph, it's the 23 aircraft that we are receiving are being offset by 23 aircraft that we are returning. So the total number of jets is actually staying the same, but with a significant renewal because we are going to have -- we are moving from 21 A321s to 36 A321s and from 10 new technology widebody aircraft to 18 new technology widebody aircraft at the end of 2015.

And that continues for 2016, where we expect to end the year with 50 A321s and with 30 new technology widebody aircraft. All of this is consistent, obviously, with our cost focus because it allows us to have a lower cost per ASK operation, and with our passenger experience because it allows us to provide an upgraded product for our passengers.

That concludes the comments that we have prepared for today. I want to mention who is available here to take your questions. We are joined by Claudia Sender, who is the CEO of TAM; Andres Osorio, the CFO; Andres del Valle, who is in charge of corporate finance, and Nicolas Goldstein, who is in charge of the international passenger operations.

We will be happy now to take any questions you may have.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Michael Linenberg, Deutsche Bank.

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### Catherine O'Brien - Deutsche Bank - Analyst

Good morning. This is actually Catherine O'Brien filling in for Mike. Just a couple questions here.

With regard to your plan to begin serving more regional airports this year, do you see more demand strength out of some of those markets versus the weakness we have seen out of the Brazilian network in 2014? Or is the decision to add regional markets more of a long-term decision to enhance Brazilian network for the future?

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### Claudia Sender - LATAM Airlines Group SA - President, TAM

Good morning, this is Claudia speaking. I think it is a little bit of both. Add it to something else, which is what Gisela was mentioning before, which is our network strategy.



So first of all, we see a few markets that today we don't serve that currently have strong corporate demands, whereas see some of the markets that we serve where the corporate demand is reducing. So it's very interesting for us to tap into these markets, because it's new additional corporate demand that we are bringing into our systems while we are still serving well the markets where we are present. So that is the first thing.

The second, as a long-term strategy, building on what Gisela said before, we do believe that we -- as LATAM Airlines Group we want to be the best option for any passengers flying to, from, or within any city in Latin America. Therefore, we need to cover the most relevant growth and these cities are growing much faster than the trunk routes, as we call them. So it is very important for us, in the long run, to have a strong presence in some of these cities.

Of course, we are prioritizing and looking into the higher GDP or higher corporate traffic routes and this is where we are starting.

I think, if I may add another point, as Gisela also mentioned, with all of these routes if you want to have an efficient -- for all of these cities, if you want to have an efficient flow coverage, we need to connect them with our hubs. So Brasilia has become very important in our strategy to make sure that these cities are not only connected point-to-point with those cities in the domestic territory, but most of all that they have access to the entire Brazilian territory but also to our international network.

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**Catherine O'Brien** - Deutsche Bank - Analyst

Okay, great. Thanks. And then just a question on costs. Your cost performance is impressive this quarter and I just was wondering how much of the decline in your operating costs, excluding fuel, would you attribute to the benefits from depreciating currencies versus the cost cuts associated with your \$650 million program?

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

If we leave aside I think the fuel benefit, probably I would say half of the rest has to do with depreciated currencies and the rest has to do with other various in part initiatives that we have already launched: the lower cost, the benefits of a more modern fleet, which has a lower cost per ASK, and then a series of other effects. But definitely the devaluation in local currencies for the cost portion that is not denominated in dollars is significant.

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**Catherine O'Brien** - Deutsche Bank - Analyst

Okay, great. If I could sneak one quick one more in, have you noticed any changes in the demand environment for the worse or the better in any countries you serve in South America from the December quarter into the March quarter?

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Well, what we've seen -- I will let Claudia talk a little bit about Brazil, but when we talk about the other parts of the operation, I think what we are seeing in general is that demand has been healthy. We are seeing that, at least in a large part of our operation, the devalued currencies in part have meant that airlines are not really willing to pass through in terms of prices a lot of the declines of the fuel price, because on the other hand they are seeing a more expensive cost structure as a result of the devalued local currency.

So that has meant that yields have remained more or less stable in local currencies, and that even with that, demand has remained healthy. So if you look at our traffic figures for January and February, this is more or less the trend that you are seeing. Overall for January and February our traffic is up by 4.6% overall, which is almost 5% in our domestic Spanish-speaking countries and more than 5% on international operations with load faster increases throughout the network.

Claudia, want to talk about Brazil?





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**Claudia Sender** - LATAM Airlines Group SA - President, TAM

Just an additional comment for Brazil. We have seen the same trend as the fourth quarter last year, which is a very depressed corporate demand due to the low GDP growth and, I would say, all the uncertainty regarding our economy and the exchange rates. So we don't see a major change in the trends that we have seen in Q4 last year.

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**Catherine O'Brien** - Deutsche Bank - Analyst

Okay, thank you so much for all the color.

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**Operator**

Duane Pfennigwerth, Evercore ISI.

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**Duane Pfennigwerth** - Evercore ISI - Analyst

Good morning, thanks for the time. I wonder if you could help us simplify the margin expansion story for 2015. Are you seeing margin expansion in all regions offsetting margin declines in Brazil, or are margins actually expanding in Brazil despite all the noise and volatility and, frankly, overemphasis on that market for you?

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

I think it's important to mention that we are not expecting during 2015, at least in this guidance number, an improvement in revenues per ASK overall. First of all, our margin expansion is driven by mostly reductions in terms of costs. And important part of that has to do with fuel, of course, and then also an important -- another very important part of that has to do with the fleet efficiency initiatives, the other efficiency initiatives that we have identified, and the devalued local currencies, which have a positive effect on costs.

So I think in all of our operations we will see margin expansion coming from a more efficient cost structure. Then we are going to see in terms of revenue per ASK probably different impact in different parts of the network, but overall I think the trends that we saw or that we are seeing during the fourth quarter and we are seeing during the first quarter is still one of revenues per ASK decline.

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**Duane Pfennigwerth** - Evercore ISI - Analyst

Understood, but I guess the question is, again despite all the noise and the volatility and the emphasis by everybody on the Street on Brazil only for your company, are you actually seeing margins up in Brazil?

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**Claudia Sender** - LATAM Airlines Group SA - President, TAM

Duane, sorry, we don't disclose margin by business so it's hard to comment on that. I'm sorry.

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**Duane Pfennigwerth** - Evercore ISI - Analyst

Okay, no problem. Can you quantify maybe the fuel savings that you expect in 2015? Maybe a \$900 million number. Is that net of your hedges, and how much of that \$900 million do you think you get to keep?

And maybe you could sort of give some regional color on that. Maybe you are holding it more effectively in markets like Peru and Chile than you are in Brazil.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Well, the total savings -- we consume approximately 30 million barrels of fuel per year, so if we look at current fuel prices at \$65 jet fuel, that's basically versus last year a savings of \$48 per barrel, which means more than \$1 billion in terms of savings. So we are talking about very significant savings if we just adjust the price of fuel.

In the different markets, there's different lags in terms of how quickly we are able to see that fuel price reduction reflected for us, so there's a little bit of a delay in all of the markets. It's longer in some markets than in others, but overall we see that decline passed through to the price that LATAM pays to consume that fuel.

The hedge estimate that we have, which is what was shown on the other slide, is that we would expect a loss in our current hedge position of approximately \$215 million. So with that \$215 million we're still expecting over \$1 billion in terms of fuel savings for the full year.

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**Duane Pfennigwerth** - Evercore ISI - Analyst

Okay, that's great. So over \$1 billion in savings and if you had to guess, how much of that do you actually keep?

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Well, over time I think -- it varies, let's say, in the first quarter towards the end of the year. So far, as I mentioned, I think in the countries, in the domestic operations outside of Brazil in general, we continue to see -- we haven't seen a downward pressure significantly in yields as a result of the lower fuel prices. Yes, as a result of the devaluation of the currencies, which impact your yield in local currency, but overall we are still seeing during the first quarter that we are seeing the benefits of that lower fuel price.

And I'm going to let Nicolas talk a little bit about the trends we are seeing in the international part.

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**Nicolas Goldstein** - LATAM Airlines Group SA - CEO, Long Haul Business

What we can capture is very different depending on the business. On the long-haul business, with the anticipation that we have, we observe a huge capture of the benefit for the first quarter. Also in the regional business, as long as you move to more domestic business with a shorter anticipation, the benefits are lower. But up to now we observe for the first quarter very good results.

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**Duane Pfennigwerth** - Evercore ISI - Analyst

Okay, thanks for the time.

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**Operator**

Bernardo Velez, GBM.



**Bernardo Velez** - GBM - Analyst

Good morning, guys. Thanks for taking the call. I was wondering if you could provide us with a little bit more color on the taxes in Brazil, and especially this -- there have been rumors that President Rousseff is thinking about cutting back the Brasil Maior program.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Yes, that's correct. Nothing has been defined yet, so what we are seeing is that there would be a change in terms of a tax that's currently over as a percentage of revenues that it would be a percentage of payroll. But nothing has been defined yet, so we can't really say anything until we have a definite ruling on that initiative.

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**Bernardo Velez** - GBM - Analyst

Okay, perfect. In another topic, could you comment on or could you give us an update on the airline unification process that you guys are going through?

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Are you referring about between LAN and TAM about merger?

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**Bernardo Velez** - GBM - Analyst

Exactly, yes.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Well, I think that we have really completed the -- in terms of the integration of the operations, I think we -- as you know, we continue to operate with two separate brands. But in terms of all of the corporate functions, we have really completed, and I'd say even before 2014 we have completed, most of the integration. And we had captured, or at least implemented, all of the initiatives that we had identified in terms of really being able to see the synergies on the cost side as well as on the revenue side from joining the networks of the two airlines.

I think probably a relevant thing to mention is that this year we had finally -- we are now operating as of January on the same ERP. So previously we were in a situation with LAN on running SAP and TAM running a different platform, and today both LAM and TAM are both on SAP. So that was one of the things that had been pending and that is today already in place.

And I would say, outside of that, there is maybe a couple more implementations that we need to do in terms of the information technology side, but for the most part the integration today is complete.

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**Bernardo Velez** - GBM - Analyst

Okay, perfect. Thanks a lot, guys.

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**Operator**

Tom Kim, Goldman Sachs.



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**Tom Kim** - *Goldman Sachs - Analyst*

Good morning. I was wondering if there has been any change in the corporate travel trends that you have been observing before.

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

In corporate demand in Brazil?

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**Tom Kim** - *Goldman Sachs - Analyst*

Yes, Brazil and then also ex-Brazil.

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**Claudia Sender** - *LATAM Airlines Group SA - President, TAM*

Let me start from Brazil. We haven't seen change, unfortunately. We would have loved to see demand picking up, but demand keeps -- remains at a drop around 15% versus same quarter last year. So we don't see great changes, but still at a depressed level.

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**Tom Kim** - *Goldman Sachs - Analyst*

And then how about ex-Brazil around the region?

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**Nicolas Goldstein** - *LATAM Airlines Group SA - CEO, Long Haul Business*

Yes, in international business we don't see any huge change in the demand on the corporate people. We haven't found any unusual change.

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**Tom Kim** - *Goldman Sachs - Analyst*

Okay. Just to be sure that my understanding is right; the traffic growth that we are seeing is still largely being dominated by leisure. Is that fair to characterize the recent growth?

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**Claudia Sender** - *LATAM Airlines Group SA - President, TAM*

For Brasilia, but the goal is deriving from the leisure traffic.

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**Tom Kim** - *Goldman Sachs - Analyst*

Okay, that's helpful. Then I guess, speaking on Brazil and the push into increasingly regional travel, at what point -- or even with the Brasilia initiative, how does stage length get affected by this? Would we actually potentially see shorter stage length and, therefore, the uptick in overall unit pricing?

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**Claudia Sender** - *LATAM Airlines Group SA - President, TAM*

I would say that the (inaudible), considering that we have already over 800 flights a day in Brazil, this is very marginal. So you wouldn't see a big change in our stage length or in our [rack] structure.

**Tom Kim** - *Goldman Sachs - Analyst*

Okay, thanks a lot for that. Then just my last question was with regard to your fuel hedging. Can you give us the level at which you have hedged for this year, what the price was?

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**Nicolas Goldstein** - *LATAM Airlines Group SA - CEO, Long Haul Business*

It's very different throughout the quarters versus by year, but no [adjusted there]. As the money for Q1, as we said that we expected conversation for this year is in region of about \$250 million. That is to the bad side. We saw also the benefits.

But it's very different from month-to-month, but overall is at \$200 million loss for the year. But that would -- again we have -- that is half of this is roughly in the Q1. So it is a very different -- happy to give you more color by email, but it's very different from quarter to quarter.

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**Tom Kim** - *Goldman Sachs - Analyst*

Okay. What I was referring to more specifically; it's helpful to have the dollar figure, but I was just wondering more from a dollar per gallon or even dollar per barrel. However -- whatever you think is best, easiest for us to be thinking about that.

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**Nicolas Goldstein** - *LATAM Airlines Group SA - CEO, Long Haul Business*

Look at Q1 as an example. Including hedge you would have something like \$83 a barrel, including hedge. And (inaudible) going down as the other quarters kick in.

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**Tom Kim** - *Goldman Sachs - Analyst*

Okay, great. Thank you very much.

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**Operator**

Savi Syth, Raymond James.

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**Savi Syth** - *Raymond James - Analyst*

For the cargo side of the business, I was just kind of curious as to how yields are trending so far in 1Q and how demand has been. And then on the fuel impact, is there a lag or what we saw in 1Q is kind of an immediate pass-through of the lower fuel?

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

Well, in terms of yields, we are seeing yields negatively impacted, so yields continue to trend downwards. In cargo, we see demand that continues to be weak with -- following the trends that we saw basically in the last few quarters and we don't really see a change in that trend for the better so far.

And in terms of fuel, the cargo business follows the same logic as the passenger business. So in Brazil, there's a longer period of time or there is a bigger lag, let's say, between when the market prices go down and when that gets priced in for the airline consumption.

In the US, it's shorter; in Chile, it's somewhere in between. So it depends a lot by market and follows the same logic than the passenger business. So probably around (multiple speakers) overall.

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**Savi Syth** - *Raymond James - Analyst*

Okay, got it. Then just on the leasing that has been done with the three aircraft, is the revenue from that -- is that flowing through the cargo revenue? Or is that flowing through other?

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

No, it's in other revenues. It's in other revenues, so not in cargo nor in passenger. And it basically isn't really -- it's not additional revenue either. It's basically a revenue that offsets the fleet costs that we had associated to those planes.

So basically what we are seeing is being able to get rid of these planes, so to speak, so that someone else is paying the fleet costs associated to them.

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**Savi Syth** - *Raymond James - Analyst*

Okay, got it. Then one last question, just going back to the domestic Brazil market. As Claudia mentioned, corporate demand is really weak and it seems like the flat capacity outlook, maybe it's a little optimistic given the market and given how much the real has declined. Especially it seems like it's offsetting some of the fuel declines in domestic Brazil.

Curious at what point could we see adjustments to the capacity plans? Or you think that the current capacity is sufficient or capacity level is sufficient to offset those headwinds?

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**Claudia Sender** - *LATAM Airlines Group SA - President, TAM*

Let me try to answer your question in two parts. First, we have to be flexible. At this point the volatility is so high that trying to make plans for the next nine months is currently a very big challenge. So we've tried to maintain flexibility while lowering our costs and controlling very closely all of the variables that we control, such as our punctuality, our level of service, and our costs.

This is the first thing; it's very hard to make any forecasts different than what we have today. We decided to fix our strategy and follow the market very closely and take action when required.

The second thing, which I really believe in, is that our strategy of covering Brazil through our main hub is very cost efficient and will give you clarity to support the strength that the LATAM network needs and that the Brazilian passenger needs. We are tapping into new markets that we didn't have access to before. We have strengthened our partnership with Passaredo, which is a small regional player here in Brazil. And by doing that, we have increased the number of locations that we serve and we are serving them in a much more cost-efficient way.

So I strongly believe that we will find new markets and we will find ways of improving our RASK through addressing corporate markets where we weren't present before.

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**Savi Syth** - *Raymond James - Analyst*

Okay, got it. Very helpful. Thank you, guys.

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**Operator**

Stephen Trent, Citigroup.



**Kevin Kaznica** - Citigroup - Analyst

This is Kevin Kaznica stepping in for Steve. Just most of our questions have been answered, but I just falling back on some of the stuff that you mentioned during the presentation and prepared comments. I guess coming back to Brazil's regional airport plan, dovetailing into that and your plans to use A319s to service that. How many regional airports I guess, if you know, as a percent can service A319s without any additional infrastructure buildout?

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**Claudia Sender** - LATAM Airlines Group SA - President, TAM

There is a very big number of airports that we can still serve. The regional airport plan is still being developed, so it's hard to know exactly what are the locations that will receive the investments for the new regional airports. But we are still looking into what is the long-term model for serving the regional locations.

For now, we will serve them with our current fleet and we can still expand quite significantly the number of airports that we serve today with the current fleet.

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**Kevin Kaznica** - Citigroup - Analyst

Got you, got you. And would you know offhand how many I guess potential airports or what percentage can't handle an A319?

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**Claudia Sender** - LATAM Airlines Group SA - President, TAM

I would say more than 20%, so we are talking about four to five new airports or new cities covered per year. So we shouldn't have a problem in the short term.

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**Kevin Kaznica** - Citigroup - Analyst

Okay, thank you very much. Then I guess, I think you already mentioned this, but it seems that American Airlines at least seems to be pulling back some of its LatAm capacity. What kind of Latin American capacity trends are you seeing from Delta, United, and others?

Is that what you were alluding to when you said the majority of those carriers were pulling back capacity from Latin America and that's kind of a tailwind for you guys?

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**Nicolas Goldstein** - LATAM Airlines Group SA - CEO, Long Haul Business

On the international market, going from South America to North America, we are observing a reduction on the offer from -- especially from American Airlines and other carriers reducing the capacity that they have. But we are also observing that from Europe to South America. It reflects that the industry is going to start reducing -- managing a little bit the offer, because if not, we are going to impact the yields.

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**Kevin Kaznica** - Citigroup - Analyst

Okay, okay, thank you very much. And then finally, just coming back to the fuel hedging, how do you guys traditionally hedge fuel?

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**Unidentified Company Representative**

How we traditionally hedge fuel you are saying?

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**Kevin Kaznica** - Citigroup - Analyst

Yes, or what strategy do you use?

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**Unidentified Company Representative**

Okay, typically we have -- we split the fuel pass-through something along the lines of about 30% that we pass on to consumers. As for rest, we enter into financial hedges typically covering nearly 50% to 60% of the upcoming quarter with a combination of colors and swaps and three ways and four ways.

As of late, we are seeing that we also are trying to protect on the downside, given the sudden losses that we have seen for the jet fuel. But in general it's a decline in scale from 50% then decreasing as time goes on.

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**Kevin Kaznica** - Citigroup - Analyst

Okay, great. Thank you very much.

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**Operator**

[Joe Mora], Bank of America.

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**Joe Mora** - BofA Merrill Lynch - Analyst

Thanks for the call. A few questions. First, on Open Skies agreement in Brazil. I would like to know if you guys could provide some more color on the outlook for yields once the agreement becomes fully operational in October. We know that the international routes yields are already under pressure, but I wonder if we could see an acceleration on that once the agreement becomes operational.

And second thing, on cash generation and on your leverage levels, we know that you have some relevant CapEx commitments for this year. I wonder if you could provide some color on what should we see for leverage [ranges] throughout 2015. Thank you, that's it.

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**Nicolas Goldstein** - LATAM Airlines Group SA - CEO, Long Haul Business

I'm going to take the first question about Open Skies. What we observed is that before Open Skies American companies start adding capacity and this is the same capacity that they are withdrawing now. So looking forward, due to the market conditions, we don't observe huge changes in the offer that we are going to observe with the open skies.

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**Unidentified Company Representative**

In front of that leverage we see -- if we added up the year 2014 with a margin of roughly 4.1%, as you shared, we have provided guidance for 2015 to be between 6% and 8% of the operating margin. So as we also heard, the margin expansion is coming from the cost reduction basically. And then, as soon as the different quarters kick in, you see a rapid deleveraging of the Company at the current levels. Again, driven by margin expansions.





On the fleet side, the total commitment is something like \$1.8 billion, but only half of that is going through debt. The rest is just a ramp-up of the leases. So we see, number one, the levels of debt being sustained and even decreased during the year and in the Q we see a good liquidity and also a shortened debt constraint at the minimum levels.

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**Joe Mora** - BofA Merrill Lynch - Analyst

Okay, that's great. If I could just follow up on regional aviation, I know that Passaredo has close to 2% of Brazilian domestic market and it's a very involved player. So regarding your strategy, should we see just, let's say, a marginal increase in the roads right now and perhaps after all the investments, after all that more than BRL7 billion that the government is planning to invest in regional aviation is deployed, then we should see a significant increase and perhaps some fleet restructuring perhaps that you could add your regional jets.

My question is actually right now this should be very small. This should be even smaller than the 2% of (inaudible) that Passaredo has. And then just after those investments that should see regional aviation really become the relevant, more relevant thing for (inaudible) in Brazil, is that so? Is that the way we should see? Thanks.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Could you repeat your question? I didn't get the last part, if you don't mind.

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**Joe Mora** - BofA Merrill Lynch - Analyst

No problem. I wonder if you could elaborate more on your partnership with Passaredo in order to -- it's a small player, they only have 2% market share. And I wonder if right now regional aviation should be very small for TAM and then just after the investments on all the airports are deployed, then we should see, let's say, the strategy becoming more relevant. Then we should see perhaps fleet restructuring. You cut all the regional jets and this could become more relevant thing for TAM in terms of capacity. Thanks.

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**Claudia Sender** - LATAM Airlines Group SA - President, TAM

First, talking about strategy; we absolutely believe that the market will keep growing in the smaller cities faster than the bigger cities. So it is something that is embedded in our strategy. It's also important for the overall LATAM Airlines Group strategy to make sure we have relevant -- we have good coverage of all of the relevant flows.

So, yes, in the future, as the airports get developed and grow and the traffic becomes more relevant, we will probably get into more and more cities and we might have to review our fleet plan. It's not set in stone right now, but we might have to do it in the near future.

Talking about our partnership with Passaredo; it is a small player, but they do get to important corporate traffic cities such as (inaudible) for example, or (inaudible), cities that have a very relevant corporate traffic, but you cannot land with a big plane. So they act as an important feeder into our hubs and this is the partnership that we see going forward.

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**Joe Mora** - BofA Merrill Lynch - Analyst

Okay, thank you.



**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

If I could add one thing, I can -- just to put in context, the whole regional aviation in Brazil is less than 10% of the total ASKs of the Brazilian market and today TAM has a relatively small position in those routes still. But it is important to keep in context that, by definition, regional aviation is the smaller routes and it's really not more than approximately 10% of the total capacity of the market.

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**Operator**

Samuel Alves, BTG Pactual.

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**Samuel Alves** - BTC Pactual - Analyst

Good morning, everyone. I have two questions. The first, I was wondering if you could give us more detail on this roughly \$100 million of provisional reversal that generated a positive on-time effect in Q4. Can you tell us how much in performance it is bundled LATAM during 2013 versus 2014? Was it zero in the previous years?

And the second question; on the other operating expenses line, the release attributes the decline to the prescription and other reversals of tax contingencies. Can you please tell us how big was this effect? Thank you.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

In the other operating expenses, the effect was approximately \$70 million. This sort of prescription and reversals of tax contingencies. And regarding your first question, I didn't get which provision you were referring to.

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**Samuel Alves** - BTC Pactual - Analyst

I was referring to the provision that generated the positive effect in the first line of the operating expenses line that you described in the press release.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Okay, wages and benefits?

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**Samuel Alves** - BTC Pactual - Analyst

Yes, exactly.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

So that was -- basically, we have performance bonuses for all of the employees in the Company and that is a cost that is provisioned on a monthly basis for the year, assuming that 100% of the goals are met. And basically, as a result of the results -- the financial results for 2014, which didn't meet a 100% of the goal that we had, we had bonuses that were lower than what we had provisioned and that generated this reversal of \$100 million.

**Samuel Alves** - *BTC Pactual - Analyst*

Okay, thank you.

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**Operator**

Renato Salomone, Itau.

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**Renato Salomone** - *Itau BBA - Analyst*

Thanks for taking my question. I would like to ask about the significant drop in commissions to agents. Could you please elaborate how much of this 47% contraction came from FX, the devaluation, and how much came from other initiatives?

And regarding these other initiatives, could you please describe some of them and how much are there to stay, or if some of these were one-off negotiations that you had adjustments at the end of the year that we shouldn't see a level, such a low level going forward? That's my question, thank you.

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

In terms of commissions, we had a series of different effects. First, in part -- so even though as a percentage of -- since revenues were down, commissions are a percentage of revenues. A part of a decline in commissions is related directly to decline in revenue.

In addition to that, for all of the domestic operations there is a positive effect from the devaluation of local currencies, which also has a positive effect. And then another part of it is point-of-sale mix, so we have different commission levels in different countries. Specifically, regarding the Argentine market, where we had a reduction in our sales, that resulted in a decline in the total percentage of commissions because -- as a result of lower sales than what we had estimated in the Argentine market as a result of the devaluation last year.

Then finally, there was another part of it that represents approximately \$14 million in the fourth quarter, which was a recovery of taxes in Brazil. So there's -- basically when you account for a certain cost you account for them with taxes and then there's a recovery of certain taxes that occur at the end of the year or at different months throughout the year. And those are accounted for in the line where the costs are. So part of that during this quarter affected commissions to agents in the range of \$14 million.

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**Renato Salomone** - *Itau BBA - Analyst*

Thank you. But on top of this, is there any major negotiation going on with agents that lowered this line or no?

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

No, no, absolutely not.

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**Renato Salomone** - *Itau BBA - Analyst*

Okay, thank you.

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**Operator**

Duane Pfennigwerth, Evercore ISI.



**Duane Pfennigwerth** - *Evercore ISI - Analyst*

Thanks for taking the follow-up. Sorry for stretching out an already long call. Just a couple quick ones on your loyalty plan. Has there been any change in your ownership percentage from that 73% level?

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

No, no change.

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**Duane Pfennigwerth** - *Evercore ISI - Analyst*

Okay. And then how much multi-plus cash is consolidated on your balance sheet in your \$1.5 billion? How much of that \$1.5 billion is actually multi-plus cash?

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

We consolidate 100% of multi-plus, so --.

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**Unidentified Company Representative**

Which was \$450 million roughly as of the end of December last year.

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**Duane Pfennigwerth** - *Evercore ISI - Analyst*

\$450 million?

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**Gisela Escobar** - *LATAM Airlines Group SA - Corporate Controller & IR Officer*

Yes.

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**Unidentified Company Representative**

Roughly, yes.

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**Duane Pfennigwerth** - *Evercore ISI - Analyst*

Okay. Thanks very much, guys.

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**Operator**

I would now like to turn the call over to Ms. Escobar for closing remarks.

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**Gisela Escobar** - LATAM Airlines Group SA - Corporate Controller & IR Officer

Thank you all very much for participating in the call today. If you have any follow-up questions, feel free as always to reach out to us directly. If not, we will see you on the next call. Bye. Have a nice day.

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**Operator**

Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect. Have a good day.

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