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FINAL TRANSCRIPT

Chorus Aviation Inc.

First Quarter 2017 Earnings Analyst Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen. My name is Sally (phon), and I will be your conference Operator today. At this time, I would like to welcome everyone to the Chorus Aviation Inc. First Quarter 2017 Earnings Analyst Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question during this time simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question press the # key. Thank you.

I will now turn the conference over to Nathalie Megann, VP, Investor Relations. Please go ahead.

Nathalie Megann — Vice President, Investor Relations, Chorus Aviation Inc.

Thank you, Sally. Hello, and thank you for joining us today for our first quarter 2017 conference call and audio webcast. With me today from Chorus are Joe Randell, President and Chief Executive Officer, and Jolene Mahody, Executive Vice President and Chief Financial Officer.

We'll start by giving a brief overview of results, then go on to questions from the analyst community.

Because some of the discussion in this call may be forward looking, I direct your attention to the caution regarding forward-looking statements and information which are subject to various

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risks, uncertainties, and assumptions that are included on Page 4 of our Management's Discussion and Analysis of the results from operations of Chorus Aviation Inc. for the period ended March 31, 2017, the Outlook section, and other sections of our MD&A where such statements appear.

In addition, some of the following discussion involves certain non-GAAP measures, including references to EBITDA, adjusted EBITDA, and adjusted net income. Please refer to Section 15 of our MD&A for a discussion relating to the use of such non-GAAP measures.

I'll now turn the call over to Joe Randell.

Joe Randell — President and Chief Executive Officer, Chorus Aviation Inc.

Thank you, Nathalie, and good morning, everyone. And thank you for joining us.

This morning, we held our annual and special meeting of shareholders. I am pleased to report that all orders of business were approved by our shareholders, and I thank our investors and our board for their support.

We've had a positive start to this year and delivered solid earnings in the first quarter. Quarter over quarter we generated an increase in adjusted EBITDA of approximately 6 percent.

Our growth and diversification strategies are taking hold, as evidenced by our recent announcement of our intention to acquire six ATR 72–600s, of which three are on lease to Flybe, a UK carrier, and three are on lease to Virgin Australia. This not only adds two well-established customers to our growing pool of airline lessees; it also expands our fleet composition to include ATR aircraft.

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Given that Chorus Capital … Chorus Aviation Capital was only formally established in January, I'm very pleased with our progress to date, bringing the anticipated non-CPA leasing portfolio to 10 aircraft.

I'm confident this momentum will continue, as we have several exciting opportunities in the pipeline. We are being very methodical as we assess these opportunities and are focused on making the right business decisions, first and foremost.

We are transforming our organization into a global leader in the field of regional aviation offering customers a complete suite of regional aviation services, including contracted flying; aircraft engineering, maintenance, repair, and overhaul; and aircraft leasing solutions. These strengths will grow our company, and differentiate us from the competition.

On the Jazz front, strengthening our cost competitiveness remains a priority, and we have and continue to reduce our costs in many areas. In the first quarter, 96 pilots transitioned over to Air Canada under the pilot mobility program, and we anticipate a total of 200 pilots will go to Air Canada this year.

Approximately 540 pilots have left Jazz through this program, retirement, or voluntary separation since January of 2015. This is a major component in our transformation, as the employee demographic is changing significantly and costs are reducing as planned.

Each of our collective agreements include industry-competitive wage scales for new entries. Today, approximately 43 percent of our pilots, 40 percent of our airports' employees, 25 percent of

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our flight attendant group, and 15 percent of our maintenance and engineering staff are employed at industry-competitive wage scales. This turnover of new employees keeps our recruiters very busy.

Our partnerships with the various aviation learning institutions and smaller airlines are providing a potential pool of new pilot candidates, and we have several other initiatives underway to support our recruitment strategy.

As we continue to transform our business and build upon an excellent foundation at Jazz, we are committed to attracting Canada's best and brightest.

We were pleased to be recognized with several awards in the first quarter that we believe makes our organization an attractive place to work for young people. These awards included being one of Canada's top employers for young people, one of Canada's best diversity employers, one of Canada's outstanding employers, one of Atlantic Canada's top 25 employers, and one of Nova Scotia's top 15.

The well-being of our employees is a priority, and these awards reinforce our pride in the practices and programs we've implemented to truly make Jazz a progressive and great place to work. I extend my appreciation and congratulations to our employees for achieving these great accomplishments.

Our operational performance in the quarter was challenged by severe winter weather that affected operations, and had the downline effect of delaying and disrupting training events for new employees, thereby impacting our on-time performance and flight completion rates.

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We incurred increased costs and also fell short on the performance incentive payment by approximately 16 percent from the same period last year.

The fleet modernization is progressing very well. This month we commenced the CRJ-900 operation, and all five new aircraft will be in the schedule by June 15th.

These aircraft will be equipped with a hot oven, Gogo wireless Internet access, and seatback in-flight entertainment systems. I have to say the aircraft look very sharp in the new Air Canada Express livery.

The team at Jazz Technical Services, or JTS, was highly productive in the quarter completing heavy maintenance checks on aircraft operated by CommutAir, a United Express regional partner, and Air Georgian and on our own aircraft. The team is highly engaged, and well positioned for more growth.

By the end of this year, we will have transitioned 68 aircraft in and out of the Jazz fleet since we amended the CPA in 2015. Our employees at both Jazz and Voyageur are experts in transitioning aircraft for induction into an operation, or preparing them as the condition lease returns.

In fact, Voyageur recently supported the transition of Q400 aircraft at our North Bay facility for another aircraft lessor. This is where we see the great potential to become a leading player in the regional aircraft leasing space. Our expertise in all areas of regional aviation is our primary differentiator from the competition.

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And the innovation continues at Voyageur. In April, we unveiled a new Dash 8–100 package freighter at a special rollout ceremony. This unique cargo aircraft has been designed, engineered, and prepared at the Voyageur Aerotech facility in North Bay. A supplemental type certificate for the aircraft was granted by Transport Canada just this past Wednesday.

The first aircraft was converted from a former Jazz Dash 8–100 passenger aircraft to a freighter configuration, and will be delivered to the launch customer, Wasaya Airways of Thunder Bay, on a long-term lease. A second former Jazz aircraft is scheduled for delivery on lease to Wasaya by the end of the second quarter. With its 10,000 pound payload, we see significant potential for this new product in the future.

In the first quarter, Voyageur Airways commenced three new contracted flying missions in Niger, South Sudan, and Sweden utilizing Dash 8–100 and -300 and a CRJ-200. We also have several outstanding bids for other new flying contracts. The MRO side of the business is also performing well, and we continue to receive positive feedback from our customers.

Our Voyageur Avparts business, where we see good growth potential, recently parted out a third former Jazz-operated Dash 8 and acquired three CRJ-200s for the same purpose.

Looking ahead, we remain determined to create additional long-term shareholder value by strengthening the foundational CPA business, growing and diversifying aircraft leasing revenues, and pursuing additional growth opportunities. So I look forward to updating you further next quarter on our transformation and growth.

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And I'll now turn the call over to Jolene, who will take you through the first quarter results.

Jolene Mahody — Executive Vice President and Chief Financial Officer, Chorus Aviation Inc.

Thank you, Joe, and good morning, everyone. Our first quarter financial performance was within our expectations, and I am pleased with our results. Here's the breakdown of the first quarter compared to the same period of 2016.

We reported revenue of 320 million, which is consistent with 2016, and is the ninth consecutive quarter of solid earnings under the amended CPA with Air Canada.

Adjusted EBITDA came in at 54.1 million, an increase of 3.2 million or 6.2 percent. The increase in adjusted EBITDA was primarily driven by increased aircraft leasing under the CPA of 4.3 million, and a 3.4 million increase related to higher margin attributed primarily to non-CPA third-party aircraft leasing and maintenance, repair, and overhaul operations.

These increases were partially offset by decreased incentive revenue of 0.9 million; decreased margin of 1.5 million related to incremental transition costs associated with pilot recruitment flow and training; increased expenses related to 0.9 million reduction in capitalized labour and maintenance costs on owned aircraft for major maintenance overhauls; and an increase in other expenses of 1.2 million.

Adjusted net income was 15.9 million, a decrease from the first quarter of 2016 of 4.4 million, or 21.7 percent. The change was the result of a 3.2 million increase that I described above,

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offset by 1.1 million increase in income taxes, 3.4 million of additional depreciation related to new aircraft, and 2.9 million of added interest cost on higher average term loans during the quarter.

Net income was 26.7 million, a reduction of 28.7 million, or 51.7 percent from the first quarter of 2016. This decrease was due to the previously noted 4.4 million decline in adjusted net income, combined with a decrease of 30.2 million in unrealized foreign exchange gains on long-term debt, 4.7 million of realized foreign exchange gains on US dollar-denominated cash held on deposit for investments in our aircraft leasing business, and 4.3 million in employee separation program costs versus the 5.5 million in signing bonuses for our maintenance employees incurred in the first quarter of last year.

While Billable Block Hours no longer directly affect our compensation, they are relevant to the rate-setting process on controllable costs and in determining controllable revenue.

The controllable revenue rates are designed to deliver the fixed-fee and infrastructure margin over an annual period if we manage our costs consistent with those assumed in the rate-setting exercise.

Based on updated planning assumptions from Air Canada, Billable Block Hours for 2017 are expected to range between 360,000 and 370,000, based on 117 covered aircraft as at December 31, 2017.

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With the continued fleet transition and the deployment of the new CRJ-900s, we anticipate the quarterly distribution of block hours to be more weighted to the latter half of the year. The actual number of Billable Block Hours for 2017 may vary from this anticipated range, due to several factors.

Our capital expenditure guidance for 2017, excluding those for the acquisition of aircraft and the extended service program of a Dash 8–300, but including capitalized heavy checks, is anticipated to range between 45 million and 55 million. We are projecting 2017 expenditures for aircraft acquisitions and the extended service program to range between 228 million and 238 million. This includes the acquisition of two CRJ1000s and six ATR 72–600s for the Air Nostrum and Avation transactions, but it does not contemplate future aircraft acquisitions.

For additional information supporting our projected guidance for the balance of this year, I'll refer you to Section 7 of the 2017 Outlook section of our MD&A for the period ended March 31, 2017.

And that concludes my commentary. Thank you for listening. Operator, we can now open the call to questions from the analyst community.

Q&A

Operator

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Certainly. At this time, I would like to remind everyone if you would like to ask a question, please press *, then the number 1 on your telephone keypad. Again, that's *, 1 on your telephone keypad.

Your first question comes from the line of Walter Spracklin with RBC. Your line is open.

Walter Spracklin — RBC Capital Markets

Thanks very much. Good morning, everyone.

Joe Randell

Good morning, Walter.

Jolene Mahody

Good morning, Walter.

Walter Spracklin

So I guess just looking a little longer term here, I know you've probably been asked this question in different ways, but you've done a great job now of diversifying your revenue base and, Joe, as you mentioned, your contract flying, your MRO, and leasing. Now where we have trouble in terms of modelling is the contract flying is set to undergo a fairly significant change or step down in 2020, but you are going to generate increasing contribution from MRO and leasing. If down the road and if you look out longer term, just in your own mind or objectives, how would you like to see contribution generally from those three? Is it still going to be predominantly contract flying with some

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additive from MRO and leasing? Or from an order of magnitude are you expecting to see a lot more from those other two?

Joe Randell

Well, I think I can just provide you with a bit of colour rather than, I guess, specific numbers. The contract flying business is performing very well, as you know. We do take a step-down in 2021 to market levels with Air Canada. And Voyageur has a successful contract flying business that we see some green shoots there with, for instance, recently launching in Europe with a contract flying opportunity.

But it's actually the growth in that area of the business is somewhat limited. We do continue to look at opportunities. We continue to work with Air Canada, et cetera. And the MRO business, while it is growing—is not a big part of our overall business—a very important one, both in terms of what JTS is doing and Voyageur and it complements the others.

But the real growth will be in the next—in the foreseeable future significant growth will be derived from the leasing business. And we raised this equity, 200 million Canadian. As you leverage it up it gets you 800 million-plus to deploy. And we've started down that road, and we're seeing some success here. And frankly, we see additional opportunities beyond what we've done to grow that business. And I see that becoming very much sort of driving the growth.

And when you look at our leasing business even as part of the CPA itself, we presently have 39 aircraft under lease to Air Canada. We'll be adding another 19 300s. We presently have 10 CAC

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third-party leases, so that is basically 68 aircraft. And the capital that we have remaining gives us enough room to look to close about maybe 20-plus more regional aircraft.

So that brings the portfolio of the leasing business to really 88 airplanes very quickly. And that puts us in a very strong number two position in the world, and we really look to grow that. So that's where you're going to see a greater shift in terms of our earnings going forward, especially as we get out to 2021 and beyond.

Walter Spracklin

Okay. And then I guess when you look at those three buckets, clearly leasing is your growth avenue, but are you looking to diversify over and beyond those three areas? Or is your attention really focused on doing what you say you'll do on the contract flying and growing the leasing business? And for now not really entertaining any other diversification initiatives?

Joe Randell

Well, we're certainly focused on executing what we have in hand and where the opportunity is. So that's clearly a focus. I think as we execute on the leasing business we will derive opportunities for the other businesses from the leasing business, because what the leasing business gives you is a worldwide network. And you end up developing relationships with operators and getting to know their businesses, et cetera. And this is where our other businesses can come in to support that.

We're really sticking to the regional aviation side as being our area of focus. If there's an opportunistic opportunity or something along the way here that makes sense in the MRO business or

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in some related business, we'd certainly be very interested in that. But in the near term we're really focused on getting our track record down in the leasing business and getting some traction on diversifying our business, diversifying the type of equipment that we finance, and diversifying our relationships.

Walter Spracklin

Okay. And then as you get out post-2020, assuming there's no major departure in terms of acquisitions or other areas of focus, you're obviously a—you generate a good level of free cash flow, and dividend is something investors have come to value in your company. As you go—now you did increase your dividend once you renegotiated the contract with Air Canada. Now the question I guess I have is coming into the step down in the contract flying with Air Canada and the ramp up in leasing revenue that you're … that along the lines of what you just said, investors given that they value your dividend, how will they wrap their head around what will drive dividend increases going forward? And is it are you generating it? Or are you looking at a certain payout ratio?

Are you looking at a certain critical mass in terms of lease revenue you want to achieve before you be comfortable in increasing the dividend? How can investors kind of look at your dividend policy and dividend increases going forward?

Joe Randell

Well, certainly in the short term … short to medium term our focus is on growing our share price. We pay out a very, very healthy dividend. The yield is, I think, certainly one of the highest in the

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marketplace over … well over 6 percent. And I believe that the real benefits here that to be derived in value from our shareholders is to see our share price increase. And in the meantime, there is a very healthy dividend.

As we move forward and what this dividend does is it does increase our cost of capital as well. We'd like to see the yield become probably more at market, and then our cost of capital will therefore reduce, and then we're certainly able to fund growth from on the equity markets and things of that nature. We have no specific plans, but that's more a general thought on our direction.

And we believe as investors start to see that this is more than just a pure dividend play, that this is a value business that has great prospects and growth opportunities, that we will see a different type of investor as well. While treating those that value our dividend with great respect, where we see the value is in transforming our business to be more diversified and to grow and for that to be represented fairly in our share price.

Walter Spracklin

Okay. Makes sense. Thank you very much for the time.

Joe Randell

You're welcome.

Jolene Mahody

Thank you.

Operator

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Your next question comes from the line of Cameron Doerksen with National Bank Financial. Your line is open.

Cameron Doerksen — National Bank Financial

Thanks. Good morning.

Joe Randell

Good morning, Cameron.

Cameron Doerksen

Maybe just a couple of questions on the recent ATR transaction; just looking at your CapEx outlook as of the end of Q1 versus where it was at the end of Q4, it looks like the ATR purchase is roughly $150 million. So I just wanted to confirm that my math is correct there?

Jolene Mahody

Yeah. Cameron, it's Jolene here. Yeah. So yeah, you're kind of looking at the difference between what we would have disclosed, I guess, and our Q4 results in that CapEx section. And included in that CapEx number is ESP, of course, and the two Nostrum aircraft and the six ATRs, so I think you've backed into the number fairly accurately.

Cameron Doerksen

Okay. And as far as, I guess, financing for these aircraft, I mean do they come with associated debt? Do you have to, I guess, find financing for them? And if that's the case, what are you seeing out there as far as attractive financing for them?

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Jolene Mahody

Yeah. No, they're coming with associated debt, and we're looking at financing very similar arrangements to what we would have done on our current fleet through EDC at similar loan-to-value ratios and similar interest ratio.

Cameron Doerksen

Okay. And as far as the, I guess, maybe the duration of the leases it wasn't disclosed, but it looks like maybe they're a little bit, I guess, shorter duration than the leases maybe on the Air Nostrum, for instance. Is there anything you can talk about as far as duration of leases? And when you look at the overall portfolio in the future, is there any sort of target range that you want to have as far as the average, I guess, lease term within the portfolio?

Jolene Mahody

Yeah. So I mean you're right that these aircrafts are a couple years old. So they're not fresh, new like we would have had on, say, the Nostrum aircraft which would come with it a longer debt financing, longer matched lease term. So they're not as long as that, but short of specifying kind of specifically what these are, given where we're looking at long term—for new aircraft we're looking at more long-term debt and lease terms, but for these not-so-new aircraft, something in the five to seven range is generally what we would look to see.

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From an overall perspective, I think in balancing we're going to look for a balance with everything we do, whether it be equipment type and manufacturer, geographical disbursement, et cetera. So all those things we'll look for in balancing the portfolio to mitigate the risk.

Cameron Doerksen

Okay. And maybe just a final question for me, just more of a modelling question. The Voyageur earn-out I think is sitting in the current liabilities. Can you just maybe give us some colour on what the timing is; which quarter that's going to fall into?

Jolene Mahody

Sure. It's second quarter of this year $6 million and then another second quarter of 2018 $6 million.

Cameron Doerksen

Okay. Perfect. I believe that's all I had. Thanks very much.

Jolene Mahody

Thank you.

Operator

Your next question comes from the line of David Tyerman with Cormark Securities. Your line is open.

David Tyerman — Cormark Securities

Yes. Good morning.

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Joe Randell

Good morning.

David Tyerman

First question just finalizing on the ATRs; so the returns on those would they be consistent with your target returns?

Joe Randell

Yes. Yes. It is consistent with our target of return on equity in mid-teens.

Jolene Mahody

Yeah.

David Tyerman

Okay.

Jolene Mahody

Which I'll just add, David, that overall equity return target is system-wide, right? Not specific detail on individual deal transaction, but system-wide.

David Tyerman

Right. Got you. Okay. Second question, on the weather you called out that it was pretty bad and I'm getting that from other places too. Can you quantify the impact that that had on the results?

Jolene Mahody

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So, yeah, and I think our disclosure kind of lays that out. So the weather was an impact in Q1 for us. Now winter operations, Q1 is generally always a little bit tough for us. It happened that last year we really came close to maxing out on all of our performance incentives. So that would have been a bit unusual for Q1 of 2016 to max out like we did. So this year was a little bit more stressful on the operation to weather, and so we saw a reduction in our incentive revenue accordingly by about $1 million.

The other factor that impacted the numbers was because of all of the heavy activity around recruitment and pilots transitioning to Air Canada, the actual weather—the weather interfered with that process and that activity driving some incremental costs that were really outside of our covered rate. So about 1.5 million or so in incremental costs related to that.

David Tyerman

Okay. So where there—

Jolene Mahody

And just to put that kind of in perspective, overall our controllable costs category for the first quarter would have been 180 million, so less than 1 percentage or about 1 percentage in cost difference.

David Tyerman

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So did this not—it doesn't sound like this had much of an effect, the weather, on profitability relative to what the CPA would be targeting. Is that the way I should be thinking about it, other than obviously there was a—

Jolene Mahody

Yeah.

David Tyerman

—substantive hit, but—

Jolene Mahody

Well, yeah, I mean we had—I think from an incentive performance perspective it's still very respectable. Earning 4.7 million in incentives is still a very good performance, and would have been consistent with what I guess our budget expectations were. And—

Joe Randell

And I did mention in my comments there that we expect about 200 pilots to flow this year. We actually had 100 of those in the first quarter.

David Tyerman

Sorry—

Joe Randell

And a big part of the training is to get employees out with training pilots—new pilots out with training pilots on the line. And once weather disrupts that training pattern then it's very difficult

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to get things back on track. So that was a disruptor for us, which is an unusual thing to have with the combination of weather and then a very high number of new pilots.

So it was a little bit of a perfect storm—forgive the pun—but that's what we had happening.

David Tyerman

Okay. So the incremental cost on the pilot flow I think was just over 1 million. Is that what you were referring to with the 1.5 million, Jolene?

Jolene Mahody

Yeah. That's right.

Joe Randell

Yeah.

Jolene Mahody

Yeah.

David Tyerman

Okay. So that sounds like it's kind of unusual; should go away?

Jolene Mahody

Yeah. I mean the activity level, as Joe said, was really quite abnormal. So we expect to have about couple of hundred pilots exit Air Canada for the year, and half of that went in the first quarter.

David Tyerman

Sure.

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Joe Randell

Now there were some stresses over the last month or so in the operation caused by the construction in Toronto. Between the end of March and May 9th, we had approximately 578 cancellations due to that and 1,000 plus delays due to the construction in Toronto, which was influenced by weather as well, but certainly not of the severity that we had in the first quarter.

David Tyerman

So 578 cancellations and 1,000 plus delays, does that have an effect on EBITDA from the CPA?

Jolene Mahody

No, controllable cancellations are what we're really measured against. Anything that's—

David Tyerman

Okay.

Jolene Mahody

—uncontrollable and related to weather and ATC shouldn't impact it, unless there's further downline implications that are more—

David Tyerman

Sure.

Jolene Mahody

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—on the controllable side that are caused by the originating weather and ATC. So it shouldn't have an effect at all overall.

David Tyerman

Okay. Okay. And then on the employee separation, the 4.3 million, is that unusual? Or should we be expecting to see further amounts like that on an ongoing basis?

Jolene Mahody

Yeah. It's a good question. So we're continuing our efforts to change the legacy workforce demographic, and I think the stats that Joe gave in his remarks as far as the penetration that we've had should populate our new industry competitive wage scales are showing that we're doing that. So we're going to continue to find—where opportunities presents themselves we'll continue to invest in these employee separation programs in order to get the new scales populated. So we'll have some continuing spend in this area.

When I look to the rest of the year—I mean this was a heavy quarter because of all the activity we just spoke of. When I look to the rest of the year, we'll probably spend about the same amount we spent in the first quarter throughout the year, and second quarter will kind of bear the brunt of that amount. So you can spread it out over the next three quarters with an equal amount to Q1 with a little bit more weighting towards Q2.

And I guess on a go-forward basis into next year I'd see a spend probably half of what we're re spending in 2017, as we continue to try and find opportunities to change the demographics.

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David Tyerman

All right. Okay. That's very helpful. Thank you. And then just to that. When you say, Joe, percentage of employees, you gave the percentages of employees in the various categories at market rates.

Joe Randell

Right.

David Tyerman

So the others, is it that they are just at high rates because they are very senior? Or were they even above the rates anyway?

Joe Randell

No. Well, these employees were with us prior to us negotiating our new collective agreements. And there were changes in certain aspects with those employees as well. But the percentages that are not covered by the percentages that I gave you are the employees that have been here for some time—

David Tyerman

Okay.

Joe Randell

—and continue to be with us. But we are continuing to see that percentage of employees covered under the new terms of these collective agreements increasing.

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David Tyerman

Okay. So it sounds like the legacy employees have a relatively high rate anyway, and that doesn't go away even with a new agreement—

Joe Randell

Yeah. I wouldn't want to overplay in terms of how high those rates are, but they generally were not covered by the new rates that we put in the agreements. And as we go forward and we work with and Air Canada on this, we knew that this transition was going to take a number of years.

David Tyerman

Yeah.

Joe Randell

And as we go out over the next couple of years you can see that the costs will be very much approaching the industry competitive rates.

David Tyerman

Okay. Understood. The last question I had was your D&A and interest costs were much larger than the revenue benefits related to them, if I interpret that correctly. I was just wondering if you could comment on that or if I'm getting something wrong on that?

Jolene Mahody

Yeah. It shouldn't be at all. I mean what we're seeing, an increase in aircraft leasing revenue under the new leases coming onboard should be fairly consistent. What you might be seeing actually,

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as I think about it, is the CRJ-900s because the CRJ-900s we took delivery of, you'll remember late last year in fourth quarter last year, and they don't actually get deployed into the CPA until second quarter. So there's a little bit of carry there without the associated revenue. So that's probably the difference, David.

David Tyerman

Okay. Okay. That's what I was looking for, why.

Jolene Mahody

Yeah.

David Tyerman

That makes sense. Okay. Thank you.

Operator

Again, if you would like to ask a question, please press *, then the number 1 on your telephone keypad.

Your next question comes from the line of Tim James with TD Securities. Your line is open.

Tim James — TD Securities

Thank you very much. Just wondering if you could talk about how your controllable costs within the CPA are tracking relative to expectations at the time of the last rate resetting? Any costs that maybe are tracking better than expected; any that are tracking a little weaker than expected?

Jolene Mahody

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Yeah. Sorry, Joe, you want me—

Joe Randell

No, go ahead.

Jolene Mahody

Okay. So yeah, so I mean we're just one quarter into our, I guess, new rates because we set the majority of our rates on an annual basis, as you know. So we just would have completed that negotiation in the first quarter, and we're pleased with where we landed.

The numbers that you would have seen kind of in the first quarter results there, the 1.5 million I referred to earlier on the pilot transitionary costs, wouldn't have been something that we would have expected to see, just because of the nature of the perfect storm that we just described between all the activity around improvements and weather. And it's not something that we expect to see on a go-forward basis repeating itself.

So we're comfortable with where our rates are and where our costs are in connection with our rates. We're continuing to see the cost-reduction initiatives take hold and pass those along to Air Canada, whether it be on the labour side with populating these new scales, or whether it be on costs related to new fleet coming in.

The one thing I'll just take the opportunity now to comment on is, I guess, the distribution of block hours does have an impact on our margin performance. And given that we're really taking these CRJs now and deploying them now, the actual block hours for the latter half of the year will be

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greater than they were in the first half of the year. And it's actually a bit different than normal because normal seasonality would see us Q1, Q4 being lower, with Q2, Q3 being the higher points in following the traditional seasonality, I guess, of a commercial airline.

But over the past couple years with the fleet transition and the way the Q400s came in last year, the way the CRJ-900s are coming in this year, that pattern is shifting a little bit. So I say that in trying to, I guess, articulate that the margin distribution doesn't occur evenly over the year. It really will be swayed depending on the production month. And so the lower block hour production month there'll be a bit of compression and in the higher margin production—or in the higher production month block hours there'll be a lift in margin. And so that has some play on how the controllable cost versus the controllable revenue plays out on an annual period.

Joe Randell

I guess the only colour that I would add, Tim, is that if you look back over the last couple of years and we anticipated a certain rate of flow of pilots to Air Canada, and I think we've stated that the faster the flow, the lower the costs go more quickly. And I think when I look at the number of pilots that we've transitioned is we're out ahead of where we thought we would be.

And of course, Air Canada derives the benefits from that in terms of the crew rates and that sort of thing. And I think when you look at our overall costs, they're coming down certainly in some areas even faster than we had anticipated a couple years ago.

Tim James

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Okay. So just to confirm then, once we're through—maybe I should ask the question, do you expect then … Based on the timing of the CRJ-900s, do you expect the seasonality by the time 2017 is complete to be a good indicator of normal seasonality? Or are you suggesting 2017 because you'll be ramping up block hours more in the second half than you normally would you're going to be unevenly distributed in terms of profitability and margins this year relative to a normal year?

Jolene Mahody

Yeah. I'd say—

Tim James

Or in the second half at least?

Jolene Mahody

Yeah. We haven't really had a normal year since we—

Tim James

Yeah.

Jolene Mahody

—started the new CPA, really, I guess is what—but I think you can look to the distribution of margin last year as a really good indicator for 2017.

Tim James

Okay. Okay. That's helpful. And then just to return to my question about your comments on controllable costs and where they're tracking—and that was very helpful—just to make sure I'm

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understanding now the way the new CPA works. Are virtually 100 percent of your controllable costs reset or the rates, I guess, reset every year at this point? So there's no sort of carryover from the original start of the CPA contract in terms of your controllable cost expectations?

Joe Randell

Well, certain costs like leasing costs and that sort of thing are certainly longer term. But generally, the rates are negotiated annually with the exception of the crew costs. And the crew costs, we did sign up with Air Canada on 10-year rates when we did the deal. Each crew cost that we charge Air Canada—of course we have 10-year collective agreements—the costs to Air Canada are adjusted, depending on how many pilots Air Canada flows, how efficient the schedule is, how many block hours are flown because all of these factors, which are not controlled by us, but by Air Canada, control our costs.

So our costs and what we charge Air Canada is adjusted accordingly, but those are rates that we—all the other, whether it's maintenance costs, airports, et cetera, it's essentially done on an annual basis.

Tim James

Okay. Okay. That's helpful. Thank you. My next question—just really a clarification—Joe, I think you mentioned up front that you expect 200 pilots to flow up this year. And did you say there's been 550 in total since the program was introduced?

Joe Randell

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So we've had 540 employees since January of 2015 have exited. By far the vast majority of those we had—I said 200 last year; there'll be 200 this year. There were actually more in 2015. The vast majority of those have flown—have gone to Air Canada, a number of others took early retirement, and a number of others just exited the organization. But that would be the total number of employees that have exited since January of 2015.

Tim James

Okay. And then my final question, just turning to the leasing business. Could you talk through how you generate the 12- to 18-month estimate for the deployment of the $200 million investment? Have you identified specific target opportunities? Or is it more of kind of a general view of the marketplace?

Joe Randell

No, we have many opportunities before us right now that we are assessing. The pipeline is full. As a matter of fact, I think we're more optimistic than we were back last fall in terms of the number of opportunities that are available to lease regional airplanes. So we're very encouraged by what we see.

So that time frame is essentially based upon the rate at which—because the capital that we have gives us enough to acquire 30, a little more than 30 regional airplanes—we've done 10—and I do not anticipate a problem in deploying this capital over the next 12 months or so.

Jolene Mahody

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So, Tim, just to add to that, if you look at the Nostrum deal that we announced last November, we had the commitments in November. So there's four aircraft associated with that. We've taken two on already. The remaining two are estimated in June and September.

So when we talk about 12 to 18 months, it's 12 to 18 months to deploy the capital. It's not necessarily at all indicative of when we'd be committing the capital, you know what I mean?

Tim James

Yeah.

Jolene Mahody

It takes time to enact those transactions to get the aircraft on property.

Tim James

Okay. And then that actually addresses the second part of that question. I was just wondering if you could give us a sense for a reasonable rule of thumb in terms of the time between reaching an agreement on the deployment of the capital 'til the revenue actually starts coming in from those lease agreements?

Joe Randell

Yeah. With Avation, for instance, we've said that we expect to close this in June, so.

Jolene Mahody

So it's really going to vary deal-to-deal.

Joe Randell

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Yeah.

Jolene Mahody

And so our best guess here when we use that 12 to 18 months is really encapsulating all of the 200 million in deployment. So it's difficult to pin it by view.

Joe Randell

And it depends on the type of deal. For instance, if it's a sale and leaseback of an airplane that's to be acquired by an operator, that order book may be some time out. So therefore it'd be some time out before you would actually have to put up the financing.

Tim James

Okay. So it's—yeah. It's not even like you could say it was 6 to 12 months because I guess there could be some circumstances where a delivery may not come for two or three years after you reach an agreement. Is that possible?

Joe Randell

Yeah. That would certainly be an unusually long time frame, but we—

Tim James

Okay.

Joe Randell

—wouldn't want to have capital sitting idle for that period of time.

Tim James

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Right.

Jolene Mahody

And that's the very nature of the 12- to 18-month time frame that we provided to have all of that capital fully deployed; not committed, but deployed.

Joe Randell

And we do have a certain amount of control over this. For instance, if you're buying a portfolio from another lessor, which is what we did in the case of Avation—you're talking about from the time you announce the deal until it closes—in that case it's roughly two months.

Tim James

Okay.

Joe Randell

So that's sort of a reasonable expectation, I think.

Tim James

Okay. So then you were indicating the 12 to 18 months is until the actual revenue or the leases begin on those so that you expect within 12 to 18 months that capital will be generating lease revenue?

Joe Randell

Yes—

Tim James

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Okay.

Joe Randell

Yes.

Tim James

Okay. That's helpful. Thank you very much.

Joe Randell

You're welcome.

Operator

Your next question comes from the line of Kevin Chiang with CIBC. Your line is open.

Kevin Chiang — CIBC

Hi. Good morning. Thanks for taking my question here. Maybe just first one just going back to Voyageur. It seems like there's been, I guess, a little bit of movement in the Northern Canadian chartered flying market. North Star Air was recently acquired. And I'm just wondering if Voyageur—or if there's an opportunity for Voyageur to deploy assets into Northern Canada? If there's opportunities to maybe grow revenue into that marketplace?

Joe Randell

Well, the focus within Canada with Voyageur is actually to lease the aircraft. We have a number of Dash 8s available for lease; we're converting some to freighters. We're parting them out,

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et cetera. We're not really—we haven't put at-risk flying on the top of our list for opportunities in Canada.

So while there may be something there, it's not high on our list.

Kevin Chiang

Okay. And then just last one for me. I'm just wondering when you think of building out this lease portfolio how your internal maintenance capabilities play a role? Is your preference to find a portfolio or lessees that will use your in-house maintenance capabilities to kind of cross-sell that? Does that play a prominent role in your decision-making process? And just wondering how that flows through in terms of how we think about maintenance provisioning on that kind of monthly lease rate? And how that's impacted by your internal maintenance capabilities?

Joe Randell

Yeah. Well, while it would be an influencing factor and we'll look out for opportunities like that, I wouldn't put a lot of weight on that. As I mentioned in my notes, we've just done transitions on Q400s for another lessor. If it happens to be required, well and good. But in the case, for instance, the ATR transaction we just did, these airplanes are deployed; three of them in Europe, three of them in Australia. And so there's really no opportunity in that particular case, but there may be others where there would be opportunity, so hard to say.

Kevin Chiang

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If I put it another way, if as you grow your global fleet of leased aircraft would you look to grow your maintenance capabilities globally as well to be where your customers are to provide that service opportunity?

Joe Randell

Yeah. We would certainly see that as being in our scope—

Kevin Chiang

Yeah.

Joe Randell

—so we would certainly look at opportunities in that area. And when I mentioned earlier about being opportunistic that's, for instance, a perfect example.

Kevin Chiang

Perfect. That's it for me. Thank you.

Jolene Mahody

Thank you.

Operator

Again, if you would like to ask a question, please press *, 1.

And there are no further questions at this time. I will now turn the call back over to Nathalie Megann.

Nathalie Megann

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Thank you very much, Operator, and thank you all for taking the time with us today.

We wish you a pleasant weekend.

Operator

Thank you, ladies and gentlemen, for your time and participation. This concludes today's conference call. You may now disconnect.

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