Chorus Aviation Inc.

CPA Amendment 2019 Conference Call

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PRESENTATION

Operator

Good morning. My name is Jesse (phon) and I will be your conference Operator today. At this time, I would like to welcome everyone to the Chorus Aviation Conference 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'd like to ask a question during this time, simply press start, then the number one on your telephone keypad. If you'd like to withdraw your question, press the pound key. Thank you.

Nathalie Megann, Vice President of Investor Relations, you may begin your conference.

Nathalie Megann – Vice President of Investor Relations and Corporate Affairs, Chorus Aviation, Inc.

Thank you, Jesse. I'd like to start by offering our apologies for the very short notice of this call. Unfortunately, we had a delay in the dissemination of our news release, so I'm very pleased that you could join us on this short notice.

With me today are Joe Randell, President and Chief Executive Officer; and Jolene Mahody, Executive Vice President and Chief Financial Officer. We'll take you through a presentation. Hopefully you've all had an opportunity to download it. It is available on our website under Management Presentations. We will start on Slide 4 where Joe will have some additional commentary to what's on the slide, and then Jolene will take you through the mechanics of our amended CPA.

Because some of the discussion on this call may be forward-looking, I direct your attention to the caution regarding forward-looking information contained in our news release dated today, January 14, 2019, and on Page 3 of the PowerPoint presentation. Joe and Jolene will now take you through the presentation and respond to questions from the analyst community afterwards. Thank you.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Thank you, Nathalie, and good morning, everyone. As Nathalie mentioned, today is truly an exciting day for Chorus. We have successfully negotiated another amendment to the capacity purchase agreement between Jazz and Air Canada. In the aviation industry, it is simply not possible to sit still. Ours is a dynamic industry and we must work together with our strategic partner, Air Canada, to seize opportunities that make both organizations stronger. Fortunately, Jazz and Air Canada have a history of doing just that.

Today we have jointly seized this opportunity to strike an even better deal, deepening the relationship, ensuring its long-term sustainability, and enhancing our competitive position. Today's announcement is a win for both Jazz and Air Canada.

As you know, four years ago, in early 2015, we also announced an amendment to our CPA with Air Canada. That move proved to be very positive for our business and for the ongoing strategic partnership between Jazz and Air Canada. It created stability in the relationship, cost reductions for both parties, enabled Chorus to further grow its Leasing business, and helped align the interest of the two companies for the future. Today we are announcing a further amendment to the CPA with Air Canada and I am pleased that once again the changes we have negotiated will secure Jazz's place in Air Canada's regional network as we extend our relationship under the agreement by an additional 10 years, out to 2035, and enhance our relevance to Air Canada as they consolidate more of their regional capacity into the Jazz footprint.

This marks the longest-term strategic partnership between Jazz and Air Canada thus far, and one of the longest CPAs in the industry. We have succeeded in addressing needed changes and commitments to our aircraft fleet out to 2035. The necessary modernization of our fleet and the commitments received from Air Canada over the term of the agreement were not available to us under the current CPA. In the current agreement, the fleet is essentially locked down by aircraft type and number for each year until 2025. The amended CPA provides more flexibility to Air Canada to effectively manage the regional route network in a changing operating environment.

The economics of the agreement are strong for Chorus, with incremental commitments in fixed fees and Aircraft Leasing revenue of $940 million and operating fleet commitments that create additional future leasing opportunity past 2025. In total, the 17-year contract will provide $2.5 billion in minimum contracted revenue, of which $1.6 billion will be generated from Aircraft Leasing. For Chorus, the amended CPA and investment by Air Canada will support the continued transformation of our business in diversifying and migrating CPA earnings to Aircraft Leasing.

You'll recall our rates under the current agreement are above market until 2020, which is why it contains a scheduled step down in rates beginning in 2021. This agreement accelerates our planned move to market-based rates in the near term as we reduce our legacy CPA fixed fees. However, we secure incremental additions to the fleet through the 2025, increase leasing opportunities under the CPA, and incremental fixed fees associated with the extended term. Further, the added owned aircraft provide us with additional tax shields that will enable significant cash tax deferrals in the near term.

One important aspect of the amendment is the introduction of an annual cap on potential controllable cost overruns. Annually, a comparison will be made between the actual costs incurred and the controllable revenue. If overall actual controllable costs incurred are more or less than $2 million as compared to the controllable revenue, a true-up will be made. This significantly reduces Chorus' margin risk, providing tremendous fixed fee earnings stability.

In connection with the amended CPA, Chorus will also secure an equity investment from Air Canada of $97.26 million. Chorus shares will be issued to Air Canada at $6.25 (phon), which represents a 5% premium to the five-day VUA (phon) as at the close of trading on January 10. On closing, it is anticipated that Air Canada will hold approximately 9.99% of our issued and outstanding shares. Chorus will enter into an investor rights agreement with Air Canada, which will include a 16-month commitment by Air Canada with limited exceptions, to hold its investment for five years, to participate into Chorus dividend reinvestment plan, and abide by customary standstill positions. Air Canada will also have a seat at the Chorus Board and intends to nominate Mike Rousseau, Air Canada's Deputy Chief Executive Officer and CFO. I look forward to welcoming Mike to our Board, as his expertise will be truly valuable as we continue to execute on our growth and diversification strategy.

Taken together with the extended term of the CPA, we view this as a tremendous vote of confidence in Jazz and Chorus by Air Canada. Indeed, this provides stability and strength our strategic partnership, secures and enhances Jazz's position in Air Canada's regional network, and endorses Chorus' growth and diversification strategy. The equity investment from Air Canada will help Chorus modernize its fleet with larger aircraft which lowers per seat operating cost and addresses a growing demand in the industry. Chorus will use approximately 60% of the investment proceeds to purchase nine new larger gauge CRJ900 aircraft which, in turn, will generate additional Lease revenue under the CPA. Chorus has conditionally secured the right to acquire these aircraft for delivery in 2020.

Chorus will utilize the balance of the proceeds to grow our Leasing business outside of the CPA. In total, the $97.26 million equity investment will be levered at approximately 3:4:1 (phon) ratio to enable and enhance Lease portfolio value of approximately $400 million to $500 million and corresponding growth in our Lease revenues. Further, Air Canada is providing Chorus with preferred partner status on the operation of aircraft up to 50 seats with the right to match third-party offers. The Jazz Pilot Mobility program with Air Canada will be enhanced and continued and will contribute to further cost reductions. This is good news for our employees as well given the certainty of operations out to 2035 at least.

We expect to continue to generate the cash flow necessary to support the current dividend and remain committed to building additional value with continued growth in our Leasing business, which is further enabled with this deal. I do note that the CPA amendments and the investment by Air Canada are tied and both are effectively conditional on the ratification of amendments to the collective agreement between Jazz and its pilots, as represented by ALPA. The tentative agreement is alive with the term of the amended CPA to 2035. I extend my sincere gratitude to ALPA and the Jazz pilots for working with us on this unique opportunity to enhance the Jazz position in the Air Canada regional network. The ratification vote is expected on or before February 1 and we will have no further comment until then on this agreement.

The remaining slides have more detail and cover some of the primary changes under the amended CPA, so I will pass it over to Jolene to take you through those.

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

Thank you, Joe, and good morning, everyone. I'm going to start on Slide 4 of the presentation material that Nathalie spoke of earlier.

As you are aware, we have two primary sources of revenue under the CPA: Aircraft Leasing revenue and fixed fees related to the contract flying services we provide. The amended CPA provides for minimum contracted revenue of approximately $2.5 billion. Of this total contract value, $1.6 billion represents contracted Lease revenue and $858 million is fixed fees related to contract flying. Aircraft Leasing is driving about 65% of this contracted revenue, providing further earnings diversification, in line with our strategy.

I'll ask you to turn to Slide 5. While we do see an overall combined reduction in contracted revenue in 2019 and 2020 relative to the current agreement, the reduction is more than offset in the 2021 to '25 period by increased Leasing revenue associated with nine incremental CRJ900 aircraft which will be added to the fleet in 2020. Substantial value is created over the extension period with overall incremental revenue of $940 million being achieved under the amended agreement. In addition, there's a significant opportunity for Chorus to increase its contracted Lease revenue beyond 2025, and I'll explain this on a subsequent slide.

Turning to Slide 6, I'll provide the additional detail on the $1.6 billion contracted Lease revenue associated with the agreement. We have essentially maintained the existing contracted aircraft lease commitment to the end of 2025 which totals $980 million in Lease revenue and includes 3 Q400 aircraft leases which expire in 2023 that will not be renewed. Please note that the debt will be retired concurrent with the 2023 lease expiry so there's no residual value of exposure for Chorus. As indicated earlier, we will add nine CRJ900 aircraft leases in 2020 and the amended agreements will extend 12 Q400 aircraft leases to 2030. Combined, these leases are valued at $420 million in incremental revenue.

The amended contract also includes the addition of five more leased aircraft in 2025 at market lease rents. Because the specific type of aircraft and corresponding lease rates have not yet been determined, we've included an estimated lease commitment value of approximately $210 million attributable to these five aircraft. Added to this, we will have new opportunities to lease more of the existing aircraft to Air Canada post 2025. The amended CPA stipulates that Jazz will operate a minimum of 80 covered aircraft for the term extension of 2026 to '35. These aircraft are not laid out by specific type other than the requirement that the 80 aircraft are to be in the 75- to 78-seat range.

On average, between 2026 and 2030 we will have lease commitments from Air Canada for 33 aircraft, and on average between 2031 and 2035 we will have lease commitments from Air Canada for seven aircraft. However, during the time period from 2026 and beyond we will own 53 aircraft in the 75- to 78-seat range, assuming no disposition of currently own fleet. As such, the most likely source for Air Canada to meet its operating covered fleet commitment to Jazz is from Chorus-owned aircraft. We've not accounted for any of this opportunity in our contracted Lease revenue figures.

Also note the debt pay down associated with all aircraft leased under the CPA is concurrent with the expiration of the relevant leases. We therefore have no debt exposure on any owned aircraft operated under the CPA. In addition, 19 of our owned Q400 aircraft leased under the CPA contain put and call rights at the end of the current lease periods, which range from 2025 to 2028, and provide Chorus the ability to put the 19 aircraft to Air Canada at fair market value.

Slide 7 provides the breakdown of contracted Lease revenue over various periods. You can see in what period the incremental value of $630 million is achieved.

Turning to Slide 8, it provides additional detail on the further leasing opportunities that exist under the amended CPA post 2025 that I just spoke to earlier. You can see here the substantial number of Chorus debt-free owned aircraft that are available for lease to enable the 80 covered aircraft minimum. If Air Canada chooses not to utilize these aircraft for operation in the Jazz CPA, Chorus will pursue other opportunities, such as leasing to another operator, selling, or parting out the aircraft.

Now we will move to a discussion on the covered aircraft and contracted fixed fee revenue. Turning to Slide 9, this table lays out our minimum covered aircraft in the amended agreement and also shows the comparison to the current CPA. The amended CPA provides Jazz a minimum covered fleet commitment from Air Canada that enhances our footprint within Air Canada's regional network. The current CPA has Jazz exiting the operation of the CRJ200 fleet by 2020. The amended CPA includes the covered fleet of 15 CRJ200 aircraft to 2025, and these aircraft will be subleased to Jazz by Air Canada.

The amended CPA allows Jazz to further modernize the fleet of covered aircraft. We will be exiting the 37-seat turboprop fleet earlier than planned while increasing the number of more modern, larger gauge equipment. This will allow Jazz to continue to serve long-range regional routes and effect an increase of roughly 2% in seats from 2019 to 2025 and is an added benefit with the addition of the nine new CRJ900s in 2020.

In our Canadian operation, we have been sheltered from cash taxes to date by the use of tax depreciation on aircraft and loss carry-forwards, which has limited our cash taxes to $2 million to $4 million per year. We are now at a point where we have utilized a substantial portion of those deductions and as a result would expect to pay higher cash taxes in the future. The investment in the nine CRJ900s will provide substantial tax shelter at a rate of 25% declining balance per year. As a result, we expect the increase in cash taxes will be substantially offset by the impact of these investments. We expect current taxes to be more in the range of $10 million per year for the next number of years.

The transition of the fleet is expected to take time to implement. It starts with deliveries of five CRJ900s which will be sourced and leased to Jazz by Air Canada, expected to begin in the first half of 2019. The DASH 8-100 aircraft that are exiting the fleet are owned by Chorus and do not have any debt associated with them. We will pursue a variety of opportunities with these aircraft. The DASH 8-300 aircraft exiting the fleet are leased from third parties. All 19 owned DASH 8-300 aircraft continue to be part of the covered fleet until 2025.

As mentioned earlier, in break value to Jazz, the amended achieved a minimum covered fleet commitment beyond 2025 of 80 aircraft with at least 75-seat capacity. The amended CPA will generate a total of $858 million in contracted fixed fee revenue over the course of the agreement, an incremental value to Chorus of $310 million, as shown on Slide 10. As indicated earlier, the amended CPA includes parameters which limit annual rate erosion to a maximum of $2 million. This is a stabilizing and significant change from the current CPA which contains no protections for annual variances. The annual rate setting process will continue; however, at the end of each year, the parties will reconcile the actual controllable revenue versus the controllable costs and a true-up of any overall differences that are greater than $2 million will occur.

With this change, the previous 10-year rates set with Air Canada for crew costs are no longer valid as they are now included in this annual true-up. This annual reconciliation limits our downside and upside to $2 million and significantly enhances the stability of the fixed fee earnings. Contrasted fixed fee revenue under the amended agreement reduces by $36 million in each of 2019 and 2020 as we early-up the move to market-based fees.

Twenty-twenty-one through 2025 fixed fees are $308 million over the five-year period as compared to $325 million under the current CPA, a decrease averaging about $3.4 million per year. The 2026 to 2035 extension creates added fixed fee revenue of approximately $400 million, more than offsetting the near-term reduction with positive net present value. The contracted fixed fee revenue noted here does not include amounts related to performance incentives given they are variable in nature and are to be earned through meeting certain operational targets defined in the agreement. The measures under the new arrangement continue to be the same: on-time performance, flight completion, customer satisfaction, and luggage. Maximum available performance incentives will reduce from $23.4 million in each of 2019 and 2020, and $12.1 million in 2021 through 2025, to levels more consistent with market norms which averaged approximately $3.4 million per year over the term of the contract.

Now I will turn the call back over to Joe to summarize for us.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Thank you, Jolene. As I noted at the beginning, we're very pleased to have achieved this agreement with Air Canada and believe this deal addresses the primary concern permeating the market, being the longevity and strength of our partnership with Air Canada. The new agreement resolutely addresses this issue and provides Chorus the continued cash flows to support the dividend.

We trust investors will appreciate the tremendous value this new deal will create, assuming the conditions precedent are met. The amended CPA will address the legacy cost issues by bringing them in line with industry standards. It will set the foundation for the next 17 years from which we can continue to build our regional aviation Leasing business and support services worldwide. Air Canada's commitments are a vote of confidence in Chorus and Jazz. These commitments demonstrate that the strategic partnership between Jazz and Air Canada has never been stronger.

I would like to thank our partners at Air Canada for working with us to achieve a win-win for both parties. I'd also like to thank my Skill Team (phon) here at Chorus and Jazz for their efforts in achieving this agreement. We will remain focused in the coming weeks on satisfying the conditions precedent to this deal and will update the market accordingly. We are truly committed to delivering additional value to our shareholders, employees, and other stakeholders.

With that, we will open to questions from the analysts.

Q & A

Operator

At this time, I would like to remind everyone in order to ask a question, please press star, then the number one on your telephone keypad. Again, that is star, one in order to ask a question. We'll pause for just a moment to compile the Q&A roster.

Your first question comes from Doug Taylor with Canaccord Genuity. Your line is open.

Doug Taylor – Analyst, Canaccord Genuity Group, Inc.

Thank you. Good morning and congratulations on the new agreement. I want to start with a couple of questions about the capital required here. You mentioned you're going to use leverage along with the new equity injection to effectively have $400 million or $500 million in capital. Now, do you see that as being enough to satisfy all of your commitments with respect to the fleet through 2025 and then there may be additional capital requirements thereafter? How should we think about that?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Well, with the deal, basically 60% of the equity that we are raising we will be using leveraging it at about 4:1 to acquire the new CRJ900s. That leaves us with, aside from the capital that we presently have available for third-party leasing, roughly another $40 million, which we expect to lever 3:4:1. So, we do not have any other commitments for aircraft in the deal with Air Canada until 2025 when we do have a commitment from Air Canada to lease at least five of the larger gauge airplanes at that time. The fleet is pretty well set now in this agreement out to 2025 with the exit of these DASH 8-100s, and a considerable investment in up gauge an additional CRJ900s.

Doug Taylor – Analyst, Canaccord Genuity Group, Inc.

Effectively, in 2025 with additional aircraft, you have to make some choices then with respect to financing whatever aircraft are being added to the fleet based on those aircraft, which are not yet known; am I understanding that right?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

That is correct. We have no other obligations to provide airplanes under the CPA at this time other than those nine aircraft which will be delivered actually next year.

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

Yes. We don't intend to hold the money up to 2025. We'll do 2025 acquisitions at that time.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Yes.

Doug Taylor – Analyst, Canaccord Genuity Group, Inc.

You provided previously a schedule and some of your marketing materials or slide decks that you kind of showed the breakdown of the fixed fee versus revenue and you've updated that today, but I just want to understand this updated agreement relative to that previous schedule. I understand, so reducing the fixed fee in 2019 and 2020 to market rates. Now, the average for 2021 to 2025 for the fixed fee portion was previously $65 million; it's slightly less now. Then for the following 10 years about $40 million a year, pretty much flat or straight line. Am I thinking about all that correctly?

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

Yes, you are. Doug, that's correct.

Doug Taylor – Analyst, Canaccord Genuity Group, Inc.

That $40 million fee for the 20—I mean, I know it's a long way out, but do you consider that to be consistent with market rates then at that point? I just want to understand. (Cross talking). Go ahead.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Yes, we do. The market, generally on fixed fees, has decreased over the last number of years and it's gotten to a level, frankly, that we feel there's not a lot of room for it to go down further. The other thing that you have to consider on the fixed fee is when we compare ourselves to other operators is the risk that operators have on the costs. That's one thing that we have addressed here by having these guardrails in place so that we can never be more than $2 million off on the controllable costs. We expect then to see the full result of the fixed fee is going to the bottom line.

We believe that that is where the market is and will continue to be because we don't see anything driving up the market for fixed fees. We've seen them come down to these levels and that's why, of course, we're diverting more of our earnings into aircraft leasing. We will start to see a pickup in 2020 as a result of these nine aircraft coming in and, as we've said, when you look at our contracted revenue, 65% of those revenues come from Leasing and we take great comfort in that. It's a market that we now know and understand and believe that the quality of that revenue stream is certainly a good one. It's really been a trade-off to some extent on the fixed fee for the increased Lease revenue, which we like.

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

I'll just add one more thing to Joe's comments, Doug. The minimum covered fleet reduces from 105 to and 80 minimum in 2026 as well, so you have to take that into consideration, kind of when assessing the fixed fee level.

Doug Taylor – Analyst, Canaccord Genuity Group, Inc.

Okay.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

The reduction in the fleet, with a significant increase in the number of larger aircraft that have not yet been sourced.

Doug Taylor – Analyst, Canaccord Genuity Group, Inc.

Understood. Two more small ones for me. One: can you update us on the DASH 8-300 reinvestment or refurbishment program and if there's any changes made to that and what's remaining? Then the second, you had, as part of your previous agreement, been buying out some of the contracts for some of your, I guess, longer tenured pilots and things like that. Is there any change in your outlook and how much capital or the spending level on those types of activities as part of this new agreement? I'll pass the line. Thank you.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Yes. Well, certainly with the 300s we completed eight life extensions on the 300s, and as you can see from the fleet table, there's a continued commitment on that fleet out to 2025, so there's no change at all anticipated in the program. As we complete those aircraft, they will be leased to Air Canada. On the pilot agreement, we do not anticipate early retirement packages, etc. It's not something that we're planning on here. As we've said, now with the rates, the pilot rates are really part of our controllable revenues and costs and will be part of the true-up going forward.

Doug Taylor – Analyst, Canaccord Genuity Group, Inc.

Thank you.

Operator

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

Tim James – Analyst, TD Securities, Inc.

Thank you. Good morning. I'm just wondering if you could talk about what catalysts might occur over the long-term, really, that might drive this potential increase in additional lease extensions and renewals that you talk about.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Well, under the contract that we have here, we have a number of 75-seat airplanes that are scheduled to enter into the fleet, and those are the aircraft that are the opportunities for us going forward beyond the additional nine that we have coming in in 2020. I think Jolene alluded to that in her comments. You want to add to that?

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

Yes. Sure, Tim. Slide 8 of the presentation lays out the fleet that we have under commitment as far as leased fleet through to 2035. We've laid it out to show you kind of the end of year fleet counts that we have lease commitments for. You can see, like, between 2026 and 2030, we move from 44 aircraft being committed at the end of 2026 to 26 aircraft being committed under lease at the end of 2030; then you can kind of see it continuing along there to five aircraft under lease commitment as at the end of 2035. We have with the CPA, though, a minimum covered fleet commitment for Jazz to operate of 80 aircraft in the 75- to 78-seat range. The opportunity for us is to lease those aircraft that we own that are not currently committed under lease to enable Air Canada to meet that 80 minimum fleet commitment, and we've not accounted for any of those dollars when we talk about contracted incremental revenue. The $940 million, which $630 million is contracted Lease revenue, we haven't factored in anything beyond what we know we have in hand.

Tim James – Analyst, TD Securities, Inc.

Okay. I guess where I'm trying to go with this is just to understand, if I take the view over the long-term that Air Canada is going to keep its regional capacity flat or grow it slightly in line with GDP, whatever metric you want to use, and I want to assume that Chorus continues to be a partner with equal significance to what it is today, is it fair to assume that it's likely Air Canada will take up and use that capacity that would otherwise be declining? I mean, is that the view I need to have to kind of believe that that opportunity will get fulfilled over time?

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

Yes. I think you might be mixing up the covered fleet perhaps with the lease commitments. We have a fleet commitment that Air Canada will operate. Jazz will operate on behalf of Air Canada 80 aircraft in the 75- to 78-seat range from 2026 and beyond. We've just not named that those aircraft by type.

Tim James – Analyst, TD Securities, Inc.

Okay. I see. I see.

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

Right?

Tim James – Analyst, TD Securities, Inc.

Yes. I was getting too crossed over there. Okay. My next question, just kind of a big picture question here: what could go wrong with this in terms of where are the risks going forward? I mean, it sounds very positive getting the extension, the better visibility through 2035. I mean, where do the risks line in this? What could go wrong? What could cause earnings or cash flow to be less than anticipated?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Well, I think Air Canada itself is very healthy and they've done a tremendous job with the airline in terms of its prospects and its results, etc. As Air Canada remains healthy, we are a big part of Air Canada's network and, as a matter fact, we're growing the footprint for Jazz as a result of this arrangement and the revenues, as we've said, are contracted. There is no provision other than certain forced measures or something along those lines, which would change that. It's one of the benefits of being in a capacity purchase agreement is that generally you are protected from the ups and downs of the business, etc. This is the third time now that we have renegotiated the CPA with Air Canada.

The difference this time, I think, is that with this change now, all our costs are at market, really, with respect to Air Canada. A lot of the issues in the past have been driven by the fact that some of our costs are above market as a result of the original CPA which we entered into in 2006. Now that has been really totally addressed by this change and, as a matter fact, we've even de-risked it further, as we talked about, by having the guardrails on the rates. We feel that this is, of all the amendments that we've made, certainly the most predictable and stable approach to the business, and I think with Air Canada's investment and support as well, and coming on the Board, I think that's an indication that the issues of the past have been really addressed and that, from our point of view, this agreement has been significantly de-risked.

Tim James – Analyst, TD Securities, Inc.

Okay. That's great. Congratulations. Thanks very much.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Thanks, Tim.

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

Thanks, Tim.

Operator

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

Kevin Chiang – Analyst, CIBC World Markets Corp.

Hi. Good morning and congrats on getting this across the finish line here. Just a couple of I guess maybe housekeeping questions for me. You've noted in your presentation and in your press release as well, that it sounds like Jazz will become, I guess, a preferred partner, as you've extended out the CPA. I'm just trying to figure out, is that a measurable piece of data we can look at it? Is it based on market share or percentage of block hours that go into regional flying that has to go to you, or does it maybe reflect increasing work you'll do on their behalf? I know you do something like ground handling and some ticket agency stuff. Is there more of that to be done or is this more qualitative in nature and maybe not easily measurable kind of on a year in and year out basis?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Well, I think we are increasing Jazz's footprint as a result of this agreement. We will see CRJ200s operating beyond the original timeframes. We will see really an additional actually 14 CRJ900s because five will be entering the fleet this year, as we mentioned, which, actually, Air Canada sourced; then, of course, we have the nine that we are purchasing and leasing in 2020. By all of those measures, we are increasing our footprint and our relevance within the Air Canada network. The recognition that Jazz will be the 75- to 78-seat operator from '26 to

‘35, which is where regional operations are going, and although fleet hasn’t been finally determined, they’ve really signed up for that with us. I think all of those things are votes of confidence by Air Canada in terms of Jazz and for Chorus as well. We’ve also negotiated the arrangement on less than 50 seats where we are the preferred source of aircraft for those going forward as they are required as well, which was something that we previously did not have. Again, I think that shows an increase in the Chorus and the Jazz footprint and its relevance to Air Canada.

Kevin Chiang – Analyst, CIBC World Markets Corp.

That’s helpful. Then on the Air Canada equity investment into Chorus, you note that 40% of that capital can be deployed outside or will be deployed outside of the CPA. Just wondering, have there been any changes in your outlook, I guess, related to CAC? Have you become more bullish and so looking to raise capital to reflect that pipeline? Just wondering if anything has changed in the past few months or quarters that may require more capital to be injected into that operation.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

I believe some good opportunity is there that we’re working on right now and hope to be able to get some of these across the line before too long. I think we’ve said before that the capital that we had we were looking at mid this year. This does give us additional capital, which allows us to continue to grow that business. It’ll probably give us another six to eight months beyond that, so we’re in pretty good shape. I think given the fact that we have this capital we’re able to look at some more significant opportunities in the marketplace as well, so that’s actually helpful. What this does for us is really gives us the stability. There has been some concern about where does Jazz fit in Air Canada’s plans and how long is the relationship going to go, etc. What this does is, I think, effectively puts those concerns to bed and we are able to get on with it, and that’s what’s important to us is to grow and diversify the business.

Kevin Chiang – Analyst, CIBC World Markets Corp.

That's helpful. Maybe a last one for me, when you originally raised capital for Chorus Aviation capital, it was through converts with an exercise price of $8.25. I think you raised equity about a year later, say 18 months later, at a higher price, and now you're issuing equity to Air Canada at $6.25. I'm wondering, did you have any conversations with Fairfax as a key stakeholder given their early investment into your Leasing business? I guess, any thought that they had on equity issuance price that was I think roughly $2.00 below their exercise price?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Well, we have a good relationship with Fairfax and I think in the past we've spoken with them about the Air Canada relationship and the strength of that and that sort of thing, so I don't anticipate any problems with that and issues.

Kevin Chiang – Analyst, CIBC World Markets Corp.

Perfect. That's it for me. Again, congrats on this deal getting across the finish line.

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

Thank you.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Thank you.

Operator

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

Cameron Doerksen – Analyst, National Bank Financial

Yes. Thanks. Good morning. Just I guess maybe a few clarification questions from me. Just first on the fleet, I mean the CRJ900s. If I understand correctly, five are going to come in this year that are sourced from Air Canada, but really the ones I guess that matter from a financial modeling perspective from our perspective is the nine that you will acquire in 2020 that'll be leased. Can you maybe just talk about sort of the timing of those? I mean, is that something you expect to have fully in operation at the beginning of 2020 or are they going to kind of come into the fleet over the course of 2020?

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

Yes. Cameron, they'll come in over the course of 2020. For purposes of modeling you can assume three that come in by midyear and the remaining by end of the year, and they'll kind of be gradual.

Cameron Doerksen – Analyst, National Bank Financial

Okay. I guess a question on the preferred partner for bidding up to 50-seater flying. Can you just maybe talk a bit about how that works and what opportunities potentially there might be with additional 50-feet aircraft flying in the future?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Really, what that is, is that as Air Canada looks at requirement for aircraft in that seat range, that we would be a preferred supplier. We will have the opportunity to actually take the business if the business is there and make our decision as to whether we want to take advantage of that at that time. That's really how that works. We have no particular plans right now. I think Air Canada just wanted to get this deal with us cemented, etc., but we will be pursuing opportunities in that regard, and, of course, we do have aircraft that are coming out of the fleet, but it's a different type and style flying and so we'll be looking at those opportunities.

Cameron Doerksen – Analyst, National Bank Financial

Basically, if the economics look decent for any potential demand that Air Canada has, then you would basically have that business, but if you don't like the economics of it, some of Air Canada would then go to another bidder?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

That's exactly right.

Cameron Doerksen – Analyst, National Bank Financial

Okay. Understood. I'm just curious—also maybe a final question for me—just on how this sort of deal came together. I'm wondering if it was something that you mutually agreed to meet to make some changes or was it something that Chorus initiated or Air Canada initiated. Also, I guess, how the Air Canada investments in Chorus kind of came to pass; is that something that you guys were looking for specifically or is that something that Air Canada wanted? Just any kind of background on how this came together would be very interesting.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Well, as we said in the past, and especially since we did the last CPA amendment, we've had a very good relationship with Air Canada. We're always talking about opportunities to do things better and what's happening in the market, and the Canadian market is changing. Air Canada is seeing some of the ultralow costs there, increased competition, etc., the growth of Encore, etc. We consistently talk with Air Canada about fleet, about the fleet mix, etc., and looking to assist Air Canada and being itself more competitive in the marketplace and being a good partner in doing so. That led to discussions about where the opportunities are and how we may be able to amend our arrangement, but always in the spirit of finding a win-win solution for both sides, having to work for shareholders of both Air Canada and Chorus. This deal was a number of months being negotiated; it is complex because there are a lot of changes, etc., including, of course, the pilot agreement that goes out for the term of the CPA, so a lot of different moving parts.

There was nobody in particular, I think, that initiated other than the fact that as markets change we recognized that Air Canada needs to look at changing to address the market dynamics, and I think we're seeing regional carriers move more and more in 75 to the larger gauge aircraft, gives you a lower operating cost; some of the congestion at the airports, you get the larger gauge aircraft. I think from what we've seen, Air Canada has been using a lot of our 900s on long-haul, especially transporter routes, feeding routes like Chicago-Vancouver or Dallas-Vancouver, that sort of thing. I think the 900s seem to be very successful in addressing that market, and the DASH 8-100s are obviously older aircraft and have a higher per seat operating cost, etc. A lot of those types of things came into the discussion and I think that's where we set about trying to find how to make this work.

I think the fact that we are moving to market competitive rates on the fixed fees, I think is good for Air Canada. It helps with its cost reduction program in the near term, but then we're able to source aircraft, lease them to Air Canada, get an extended term, and strengthen the relationship. Frankly, we are still very excited about the growth of the third-party Leasing business and that's why the equity helps in terms of providing the equity for the CPA fleet and getting us an amount that we can continue to grow our Leasing business without having to go back to capital markets, etc.

Cameron Doerksen – Analyst, National Bank Financial

Okay. That's great. Thanks very much.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Okay.

Operator

Again, if you would like to ask a question, please press star, one. Your next question comes from David Ocampo with Cormark Securities. Your line is open.

David Ocampo – Analyst, Cormark Securities, Inc.

Good morning and congrats on getting the deal done. Since there is more certainty on the revenue from the CPA and the additional $40 million that you can use for CAC here, at what point does CAC grow organically now that there's more visibility there?

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

I guess, David, I think we've talked about this in the past as well, that even without this additional capital that's been raised here with 40% of it being deployed with CAC, on its own CAC is generating cash flow that can be turned around and invested in the business. That's already happening, it's just it'll happen to a greater degree. I guess as far as kind of where we take the business, we'll monitor that as we go as far as the opportunities that exist. We want to continue to diversify and we see that at a great source of diversification and earnings and it's a business that we know well and we've executed well on. As far as where we will take it, we'll see as time moves on here.

David Ocampo – Analyst, Cormark Securities, Inc.

What are your thoughts on the dividend here so you guys don't have to go to market and raise equity? Are you guys committed to the dividend for the long-term?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Basically, what we've said is that we continue to have the cash flow to support the dividend, and that's our message to the market. Any speculation or change or anything on the dividend is subject to the Board. We recognize it is important to our shareholders and it was one of the things that in making these changes we were very conscious of.

David Ocampo – Analyst, Cormark Securities, Inc.

All right. Just some quick ones here. The Pilot Mobility program, is that still based on the relative share of your regional capacity with Air Canada or has that changed under the new amendment?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Because this is part of our collective agreement and its ratification process, we’re not able to comment on that at this time.

David Ocampo – Analyst, Cormark Securities, Inc.

Okay. The incentive revenue and step down there, I'm assuming this is the same as the old agreement that you have that this does not have a real impact on your earnings since this is kind of paid down in variable comp?

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

Yes. A large portion of what we had been earning was paid under variable comp, so agreed.

David Ocampo – Analyst, Cormark Securities, Inc.

Okay. Thank you. That’s all for me.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Okay.

Operator

Your next question comes from Turan Quettawala Scotiabank. Your line is open.

Turan Quettawala – Analyst, Scotiabank

Yes. Hi. Good morning and thank you for taking my questions and congratulations on the deal here. I guess I was just—I apologize if I missed this maybe early in the presentation—but just looking at the Q400 fleet, obviously there's a change in the aircraft mix here with more CRJs coming in, so just wondering those 44 Q400s that you have in the fleet right now, those are owned, if I'm not mistaken, and that goes to '36. What happens to the rest of the aircraft? Does that sort of open up an opportunity for leasing those to third-party?

Turan Quettawala – Analyst, Scotiabank

No. Actually, of the 44 aircraft only 34 are owned; 10 are actually third-party leases that are done through Air Canada and we have the continued commitment on the fleet. There is a noted three aircraft reduction happening in 2023 where Air Canada has said that they are not interested in extending three of the Q400s beyond that date. I think there's a move, a foot here, of course, clearly to move more into CRJ900s. The CRJ900s in a lower fuel price environment give a lot more flexibility in terms of longer face lens (phon) and its adaptability to a changing network, and that's what we're seeing here in terms of the change in the fleet plans. Three of those aircraft will be coming out that we own in 2023, as Jolene mentioned, the debt will be paid off and we will be looking to remarket those airplanes at that time.

Turan Quettawala – Analyst, Scotiabank

Okay. That's helpful. Thank you very much. Just, overall, Joe, if you look at the aircraft and the fleet changes that you're making, it seems overall an increase in the capacity that you guys are going to be flying for Air Canada. Can you just give us a sense of maybe how much that's going up overall?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

I believe we mentioned in the notes there that it was about a 2% increase in seats.

Turan Quettawala – Analyst, Scotiabank

But what about, I guess, is ASM also potentially higher or not really?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

Oh. In terms of ASMs?

Turan Quettawala – Analyst, Scotiabank

Yes.

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

I would say the ASMs would be substantially more because of the type of flying that the CRJ900s would do. We have not done that calculation. Again, it depends on the fleet deployment by Air Canada, but I think the success of the CRJ900s on long-haul fee groups and, in many areas, I think this shows by Air Canada's commitment that they've been very pleased with the production of that aircraft.

Turan Quettawala – Analyst, Scotiabank

Perfect. Just a last question for me here: can you give us a sense of when you think about the third-party leasing and the growth that you're going to have over there under CAC, can you give us a sense of maybe how much of your Leasing business will be connected to Air Canada in 2025?

Joseph D. Randell – President and Chief Executive Officer, Chorus Aviation, Inc.

I believe we have that on the charts. We presently have 34 aircraft in CAC on leases and...

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

Yes. That's not—if you're looking for kind of a breakdown of revenue in 2025 between third-party CAC leasing and the Air Canada CPA contract, that's not something that we are sharing, Turan. But I think that from a modeling perspective you have all the ingredients to kind of work through the deployment of the remaining CAC capital, which is about $140 million when you add in what we have here achieved with this recent raise, and so $140 million to be deployed. As we indicated earlier, we're adding a bit of timeline to what we had indicated before, so prior we were saying mid-2019 we would have the additional funds deployed, now we're adding six to eight months to that for what we picked up here.

Turan Quettawala – Analyst, Scotiabank

Okay. Perfect. Thank you very much.

Operator

There are no further questions at this time.

Nathalie Megann – Vice President of Investor Relations and Corporate Affairs, Chorus Aviation, Inc.

Thank you very much. Then if there are no further questions, we'll conclude the call. Once again, thank you for jumping on at the last minute.

Operator

This concludes today's conference call. You may now disconnect.