

Chorus Aviation Inc.

Second Quarter 2024 Financial Results Conference Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Chorus Second Quarter 2024 Financial Results Conference Call. At this time, all lines are in a listen-only mode.

Following the presentation, we will conduct a question-and-answer session.

If at any time during this call you need assistance, please press *, 0 for the Operator.

This call is being recorded on Wednesday, August 14, 2024.

I would now like to turn the conference over to Tyrone Cotie, VP of Treasury, Investor Relations.

Please go ahead.

Tyrone Cotie — Vice President, Treasury & Investor Relations, Chorus Aviation Inc.

Thank you, Joanna (phon). Hello, and thank you for joining us today for our second quarter conference call and audio webcast.

With me today from Chorus are Colin Copp, President and Chief Executive Officer; and Gary Osborne, Chief Financial Officer.

We will begin today's call with a brief summary of the results, followed by questions from the analyst community.

As there may be some forward-looking discussion during the call, I ask that you refer to the caution regarding forward-looking statements and information found in our MD&A.

This pertains specifically to the results and operations of Chorus Aviation Inc. for the three months ended June 30, 2024, as well as the Outlook section and other sections of our MD&A where such statements appear.

As a result of the agreement to sell the Chorus Regional Aviation Leasing segment, or RAL, the RAL segment has been reclassified to discontinued operations and our Regional Aviation Services segment, together with corporate, is now referred to as continuing operations.

Finally, some of the following discussion involves non-GAAP financial measures, including references to adjusted net income, adjusted EBT, adjusted EBITDA, leverage ratio, and free cash flow.

This quarter, we have also provided certain of these measures on a pro forma basis to illustrate the financial impact of the disposition of the RAL segment on our capital structure.

Please refer to the MD&A for further information relating to the use of non-GAAP measures and pro forma figures.

I'll now turn the call over to Colin Copp.

Colin Copp — President and Chief Executive Officer, Chorus Aviation Inc.

Thank you, Tyrone, and good morning, everyone. As we just recently reported out on the RAL sale transaction, I'll keep my comments short today.

I'm pleased to report that our second quarter results with the revised comparative figures, as Tyrone mentioned, reflect a strong, steady, and reliable business going forward, with our cash generation enabling us to further improve our leverage ratio.

As we look forward, Jazz has approximately \$1 billion in contracted revenue in the form of fixed fee and leasing revenue under its CPA for the term of the agreement, and Voyageur is steadily growing.

This quarter, both Jazz and Voyageur delivered strong financial performance with a combined adjusted EBITDA of \$51 million and \$105 million year to date.

Voyageur delivered a \$4.8 million increase in revenue over Q2 of 2023, demonstrating their ability to seize new opportunities. They purchased a King Air 200 in the second quarter of 2024 in support of their contract with Air Ambulance New Brunswick with a provision of fixed-wing air ambulance services.

I'm pleased with our results and the progress we've made with improving the financial position of the business. Through the quarter, we also bought back 1.4 million common shares under our NCIB.

Turning for a moment to our recent announcement on the divestiture of Falko and our Regional Aircraft Leasing business, the process continues to progress well, with our shareholder meeting called to approve the transaction in just over a month, scheduled on September 25th.

I'm very pleased with the feedback we've received so far from our shareholders and industry partners, which further reinforces the value creation of this transaction.

We appreciate that it will take a few months for us to get through the various approvals and for the transaction to close, and that it'll also take time for the true value of our business to be reflected in our share price.

It is well recognized that this transaction will enable us to significantly deleverage our capital structure, generate more predictable cash flow, and provide us with the flexibility to grow and return capital to common shareholders going forward.

The benefits of this transaction cannot be overstated when you consider the strength of our go-forward cash flow and liquidity, in combination with the simplification and improved flexibility of our business.

On the debt side alone, we see a dramatic reduction in our pro forma leverage ratio to 1.5, and post closing we expect to eliminate substantially all corporate debt, giving us strong financial flexibility

going forward. This will create the right conditions to allow us to grow at a steady pace and capitalize on accretive opportunities in the aviation and aerospace sector.

I also recognize that our investors want to know more about the return of capital to shareholders. We appreciate your patience as we work towards the close of this transaction.

Our priorities are on shareholder returns, measured growth, and managing down corporate costs.

Over the next few months, our focus will be on closing the RAL transaction, which is subject to shareholder approval, regulatory approvals, and other customary closing conditions. We continue to expect the transaction to close before the end of the year.

As a final comment, I want to thank our employees for their hard work over the past several months and reiterate my confidence in our ability to grow at a steady pace going forward, and to thank our shareholders and Board of Directors for their support.

I'll now pass it over to Gary to take you through the financial highlights. Thank you.

Gary Osborne — Chief Financial Officer, Chorus Aviation Inc.

Thank you, Colin, and good morning.

As mentioned at the opening, as a result of the announced RAL transaction, the RAL segment has been reclassified to discontinued operations and our Regional Aviation Services segment, together with corporate, is now referred to as continuing operations.

Chorus will have one reportable operating segment and will no longer disclose its results on a segmented basis.

Our second quarter results for continuing operations were in line with our expectations, and the guidance provided for the Jazz CPA and capital expenditures remain in effect and are contained in the Outlook section of our MD&A.

As we look at the results from our continuing operations for Q2 2024, our adjusted EBITDA came in at \$51 million, in line with our expectations.

Our free cash flow was \$28.2 million for the quarter, primarily derived from operating cash flows.

Our leverage ratio was 3.0 at the end of the quarter, down from 3.3 at December 31, 2023. This has been accomplished primarily through long-term debt repayments of \$79.7 million since December 31, 2023.

Our adjusted net income available to common shareholders from continued operations was at \$0.01, which includes the debt and preferred equity costs, which we intend to eliminate at the close of the RAL sale.

We also allocated capital to retire 1.4 million shares in the quarter at a weighted average price of \$2.15 per share.

As Colin mentioned, after closing, the sale of RAL will allow us to eliminate \$1.7 billion in financing, including all RAL segment aircraft-related debt, substantially all of Chorus' corporate debt, and the US\$300 million preferred shares.

I'd like to also share some additional details on the benefits of the sale to shareholders.

Post closing, the transaction is expected to significantly improve Chorus' key adjusted metrics.

If we look at this quarter and overlay those effects on a pro forma basis, as we show in Section 4 of our MD&A, we see pro forma adjusted net income available to common shareholders per common share from continuing operations of \$0.08 and \$0.17 for the three and six months ended June 30, 2024.

This would be more than a fivefold increase in our currently reported figures of \$0.01 for the quarter and \$0.03 year to date.

Our pro forma leverage ratio would be 1.5 at June 30, 2024, half of the 3.0 reported in this quarter, demonstrating the significant financial flexibility we will have moving forward.

And pro forma free cash flow of \$32.4 million and \$67.3 million for the three and six months ended June 30, 2024, up approximately 14 percent from the \$28.2 million and \$58.9 million reported.

This demonstrates our strong cash flow that will support future return of capital to shareholders and measured growth.

The sale of RAL will allow us to make changes to our capital structure that will result in a substantially strengthened and simplified balance sheet.

Changes in capital structure will drive improved profitability, primarily driven from reduced debt-servicing costs and by eliminating the preferred share dividends, which more than offset the foregone earnings from the RAL sale.

Our pro forma leverage level will be well below the target range for the Company and that of our peer group, providing us with flexibility moving forward.

I would like to conclude by mentioning that we worked with our lenders, led by the Bank of Nova Scotia, to put in place significant flexibility in our capital structure with this transaction.

Subject to closing of the sale of the RAL segment, we have amended our \$50 million bilateral facility, secured by the unencumbered aircraft leased under the CPA to be available for future growth opportunities and general corporate purposes.

In addition, we are maintaining our \$150 million secured operating revolver. This provides us \$200 million in financing to support operations and the growth of the Company.

We are now ready to take your questions.

Q&A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session.

Should you have a question, please press the *, followed by the 1 on your touch-tone phone.

You will hear a three-toned prompt acknowledging your request.

If you are using a speakerphone, please lift the handset before pressing any keys.

Your first question comes from Hillary Cacanando from Deutsche Bank. Please go ahead.

Hillary Cacanando — Deutsche Bank

Hi. Thank you for taking my question. So it looks like you're set up very well post the transaction with more flexibility to increase shareholder value and for growth.

And so with a fixed contract with Air Canada as your major bid, I was wondering what would be the biggest risk to your story, or to your business going forward? Would it be global recession? Or geopolitical situation? Or would you say you're pretty insulated now with that as your main—with a fixed contract as your only business?

Or is there something else that could ... that you would consider a risk to your story?

Colin Copp

Hi, Hillary, it's Colin. Good morning.

Hillary Cacanando

Hi, Colin.

Colin Copp

Yeah. I think on the risk side, Voyageur and Jazz are very solid. There's almost—we're extremely insulated there with both of them. Voyageur's very diversified in what they do.

And Jazz is extremely solid with Air Canada with a long-term contract, as you know. So we don't see any real apparent risk there at all.

I think our focus is really in three areas, as we kind of reiterated over this last few weeks here. It's really about evaluating as we get through the transaction shareholder returns, looking at measured growth, and managing down our corporate costs.

Those are kind of our three areas of focus as we move forward.

Hillary Cacanando

Got it. Great. Thank you. And then I just have a question on the Cygnet business. It doesn't look like we really have a pilot shortage situation any more, I think.

So are you still seeing the same type of like interest level among potential candidates? Or do you think perhaps maybe are we in a situation maybe that we have more candidates than demand in the industry?

Colin Copp

Yeah. Yeah. Absolutely. I think in the US, we are seeing a little bit of a slowdown on the pilot side. In Canada, we've not seen that.

Cygnet continues to track very well. And as the demand, I guess, in the higher-level regionals and the mainline operators slows down, there's still a big demand in Canada for pilots at the lower levels.

So we see Cygnet continuing to grow on track, on plan. And we have no problems attracting students, new hires, or even finding placements. So we see that continuing on for a long time.

And most specifically that it's a little bit of a differentiated product with its relationship with CAE.

Hillary Cacanando

Got it. Great. Thanks for the time.

Operator

Thank you. The next question comes from James McGarragle from RBC Capital Markets. Please go ahead.

James McGarragle — RBC Capital Markets

Hey. Good morning, and thanks for having me on.

Colin Copp

Good morning.

Gary Osborne

Good morning.

James McGarragle

Hey. I've just got a longer-term type of question on the CPA. There's a step down in 2026 that you flag in your guidance. But those aircraft that come out of the CPA in that year, how do you expect to redeploy those?

And when we think about this even longer term as the aircraft come out of the CPA, is that cash flow neutral as these aircraft are potentially redeployed? If you can just provide any colour there. Thank you.

Colin Copp

Sure, James. Good morning. All the aircraft that are in the CPA as they come out, or come off that, all are basically unencumbered. I think Gary's talked about that quite a bit. And he can give you some view on kind of the financial side.

Right now, our plans are to continue to work with Air Canada and renew those leases, and we continue to make progress in that area.

So the immediate plan is, obviously, to see those aircraft continue within the Jazz CPA. And where they can't, they're basically unencumbered assets that we could either redeploy into different operations or we could sell, or we could do whatever we want with.

But given that they're unencumbered, it gives us a great deal of flexibility with regards to those assets.

I don't know, Gary—

Gary Osborne

Yeah. It's Gary here. Yeah. So if you look at our disclosures, we have nine aircraft that sit in our disclosures as coming off lease. We continue to look for opportunities, whether it's with Air Canada or others, to re-lease some of those aircraft. And if not we can redeploy them, as Colin said.

But they are unencumbered. They're debt free. And we have opportunities to redeploy or to sell in some cases. So it does provide some flexibility at least moving forward.

James McGarragle

Hey, I appreciate the colour. And then on Voyageur, some of your peers have talked about some pretty good opportunities, surveillance, medivac. Anything that you're kind of working on there in the immediate term that you can flag?

And then is this strategy discussed longer term there still appropriate? Or any updates that you might want to flag post the recent sale of the RAL business? And after that I can turn the line over. Thank you.

Colin Copp

Yes. Absolutely, James. I think when you think of Voyageur, you look at the various disciplines that they're in and that they've been successful at growing in, which really relate back to kind of the specialty aviation defence side of things and the USM side, the parts business. Those have been the two big kind of growth areas.

We continue to see opportunity in those that are quite significant. We announced there this quarter the air ambulance, the growth in air ambulance. Before that they had an additional King Air that went into Department of Defence into the major program. Those are the kind of things that you're going to see as we push forward with them. There's quite a bit of opportunity there.

And we're pretty bullish on Voyageur and where it's headed for sure.

Operator

Any further questions, James?

James McGarragle

Oh, no. That's it for me. Thank you.

Operator

Thank you. Next question comes from Fadi Chamoun from BMO Capital Markets. Please go ahead.

Fadi Chamoun — BMO Capital Markets

Yes. Good morning. Maybe one question from me on the areas of focus. Colin, you mentioned kind of as you get past the closing of this transaction and you have a strong balance sheet, you have a strong free cash flow that is generated by the remaining operation, how are you thinking about kind of the framework for capital going forward?

Like in terms of M&A and opportunity for growth, what type of assets? And maybe what is the targeted return on capital framework that you expect to deploy capital towards?

What are you targeting the potential growth opportunity, whether it's M&A or organic? Is it 15 percent, 20 percent? Just kind of to get an idea how you're thinking about that free cash flow redeployment as we get past the closing of this transaction.

Colin Copp

Hey. Hi, Fadi. Yeah. Absolutely. I think Gary said a few times, and so have I, we're focused on mid-teen returns. There's no question about that. And that's whether we're looking at organic growth, or we're looking at acquisition.

On the acquisition side, we're very much focused on kind of this paced gradual growth. Not big, huge, massive transactions. Stuff that's going to move us over time nicely. And so that could be anything that's in aviation or aerospace we're looking quite broadly at the opportunities right now.

So you'll see us definitely in that area, in that zone. Smaller opportunities that make sense that we understand well, those are kind of the acquisition side.

And on the organic side, I think I've said a few times, most of that opportunity probably lies today within Voyageur. And we've been successful at moving them along quite well. I think there's lots of growth still there.

And we see that area, especially the defence and the surveillance side as a growing business. There's no question we're seeing more and more download of that type of work from government into industry.

And so those opportunities are the areas that we're focused on.

Fadi Chamoun

Okay. Appreciate it.

Operator

Thank you. Next question comes from Konark Gupta at Scotiabank. Please go ahead.

Konark Gupta — Scotiabank

Thanks, and good morning.

Colin Copp

Good morning.

Konark Gupta

Morning. Thanks for taking my question. I just want to understand in terms of your continuing operations, so this is obviously really three things that you're focusing on: CPA, Jazz essentially, and Voyageur, plus Cygnet maybe. Obviously, Voyageur seems like it's growing nicely here we saw in Q2.

So on CPA maybe if I can ask you in terms of—and to James' question as well a little bit—you have these minimum-covered aircraft, which are obviously changing over time. You have the fixed fee or fixed margin. That's kind of it's a step-down function through 2026, and then I think it's probably flatline after that.

But the leasing revenues, the one where I think it's based on your Investor Day presentation seems like it's coming down, at least for now, through the end of the contract.

So you said you're looking to renew some of the leasing agreements with Air Canada. In terms of what's the discussion like with them? Why have they not sort of signed those lease agreements for long term? Why are they retiring them as per the plan today?

Is there something that Air Canada's contemplating to do with the aircraft on their own? Or is it just that depending how these contracts work they don't sign these long-term leases through the end of the contract?

Colin Copp

Yeah. Morning, Konark. Look, A, I'm just trying to capture what you said. It was a little hard to hear you, but I think I've got it.

Look, the leases, the Dash—it's mainly the Qs right now that you're looking at if you look at the leases that come open over a period of time here. Those are the ones that obviously we would be engaged with and working with Air Canada to renew and extend within the CPA. That's really been our focus at Jazz.

So those are the ones. I think Gary can give you a little bit of visibility as far as what we have in the MD&A and so on. So I'll pass it over to him.

Gary Osborne

Yeah. Konark, it's Gary. So we have if you look at the MD&A there, we have nine aircraft that come off officially leased with Air Canada at the end of 2025. They're towards the end of '25. So typically this is the time you'd start to consider your options around those aircraft. So I wouldn't read anything into it other than just natural timing.

So from that perspective we're looking at those aircraft. We'll see what we can do with Air Canada. We also have the option to redeploy. And we also have the option for those that don't get redeployed, or whatever, to sell them. So we've got some flexibility there.

But I wouldn't read anything into it more than we're always in discussions with Air Canada, and we continue to find—see if they need some of these aircraft for a bit.

Konark Gupta

Okay. No, that's very helpful, Gary. And ...

Gary Osborne

Yep.

Konark Gupta

Just to follow up on that, it seems like the fixed margin is a fixed margin, but leasing revenue is an opportunity for you where it may not decline to the level that people think. It might actually be flat, or it can actually go up, depending on how the discussions progress with Air Canada. Right?

Gary Osborne

So on the fixed fee, I think, Konark, the fixed fee is the fixed fee. So I would take what you have there and that would be a good number.

On the leasing, there's potential for upside. There's no question about it. We've got nine aircraft there. Maybe a potential to have some of those go back in, or re-lease them somewhere else.

And as time goes on it's the same thing. You'll see as the years go on and there's a few aircraft that come out, there's opportunities with those too, so.

Konark Gupta

Great. Okay. Thanks. And maybe last one for me before I turn it over. Voyageur, good growth in Q2. You talked about the opportunities there for the long term.

So should we think about growth in that business over the next couple of years, I think you had probably a target for that business at \$150 million-ish in revenue. It seems like it's doing about \$100 million to \$120 million a year right now. Do you have the visibility to get to \$150 million by 2025? Or it's more of a long-term story?

Gary Osborne

Thanks, Konark. It's Gary. I think we're still on pace for that \$150 million for 2025.

You see the growth that you're seeing here this year and hopefully it'll continue. And based on the things that Colin talked about, like under the MAISR contract, and a few other things like that we're starting to see growth. And it takes hold.

And with Voyageur in those particular businesses, it's a little bit of a step growth because once the contract comes online it takes a little bit, and then you start to see the full weight of it. So we feel like we can still get there.

Colin Copp

Yeah. I think the big thing for them is if you continue to see growth in the contracts, not so much the financial. As Gary said, there's always a little bit of give-and-take in all of these different contracts. And they are pretty meaningful to their finances. So you'll see some give-and-take.

But the big thing is looking for that continual contract growth, and they've been doing a great job of that. They have lots in the pipeline. So we're pretty bullish, as I said, on them.

Konark Gupta

Right. And so these step functions you mentioned, is that step function ending in '25 based on the contracts you have today? Or should we see a further ramp-up beyond '25?

Colin Copp

I think you're just—the point is you're going to continue to see the revenue go up, but it can go up in chunks as they bring in new contracts. So a good example is MAISR really came in last year, so that's starting to take effect. That's the type of thing you're going to see.

Konark Gupta

Okay. Perfect. Thanks for the question. Thank you.

Gary Osborne

Thank you.

Colin Copp

Okay. Thanks, Konark.

Operator

Thank you. Ladies and gentlemen, as a reminder should you have any questions, please press *,
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Next question comes from David Ocampo at Cormark Securities. Please go ahead.

David Ocampo — Cormark Securities

Good morning, everyone. I just had one, and I apologize if it was already asked because I actually missed a few minutes of the call this morning. But when I look at your contract with Air Canada, I know post 2026 you guys have 80 covered aircraft compared to, call it, 105 today.

When we think about that step down in fleet count, is AC looking to bring on other partners to bridge that gap? Or are you guys thinking that you could bid on that 25 extra fleet count as it relates to your fixed fee with Air Canada?

Colin Copp

Yeah. Good morning. It's Colin. As far as the CPA goes, we are very focused on opportunities with Air Canada. So any opportunities that come up you'll see us working with Air Canada on and bidding on.

We've been quite successful at getting our cost structure right and being able to really position things well with Air Canada. And if you just go back in history in the last five whatever years, you can see kind of where we sit in relation to our relationship and partners.

So we're going to continue that. We're very comfortable and bullish and supportive of Air Canada and the work we do there for them. And any opportunities that come up for growth, just like we talked about here a few seconds ago on the Dash-8s, we're working with them to see where those opportunities are and to see if we can make things work.

So I think Jazz, it has a minimum fleet there, but that doesn't mean that's necessarily the fleet that we're going to be at for sure.

David Ocampo

And I guess, how early with your discussions are you with Air Canada for that post-2026 fleet? I suspect you might need to do some pilot training if the fleet changes in a material way. So just curious where that stands today since we're edging closer to 2026 now.

Gary Osborne

Well, I think—it's Gary here, David. If you look at the 80 aircraft of 70-plus seats, they're currently in the fleet. So from that perspective, nothing really needs to change for the fleet in '25—or in 2026.

So from that perspective it is in place, it's just a question of whether it's above the 80, or what the fleet plans are. But it currently exists.

David Ocampo

Okay. That's all I had for you guys. Thank you.

Operator

Thank you. We have no further questions. I will turn the call back to Tyrone Cotie for closing comments.

Tyrone Cotie

Thank you, Joanna. And thank you, everyone, for taking part in today's call. Have a nice day.

Operator

Ladies and gentlemen, this concludes your conference for today. We thank you for participating, and we ask that you please disconnect your lines.