

AEROFLOT GROUP Q3 & 9M IFRS RESULTS CONFERENCE CALL

EDITED TRANSCRIPT

AEROFLOT GROUP SPEAKERS

- Andrey Chikhanchin - Deputy CEO for Commerce and Finance
- Andrey Panov - Deputy CEO for Strategy, Service and Marketing
- Ivan Batanov - Head of Revenue Management
- Andrey Napolnov - Head of IR and Capital Markets, Deputy Corporate Finance Director

PARTICIPANTS ASKING QUESTIONS

- Matvey Tayts, Sova Capital
- Ivan Postevoy, VTB Capital

AEROFLOT GROUP PRESENTATION

Operator:

Good day and welcome to the Aeroflot Group 9M 2021 IFRS financial results conference call. Today's conference is being recorded. At this time, I would like to turn the conference over to Andrey Napolnov, Head of Investor Relations and Capital Markets. Please, go ahead sir.

Andrey Napolnov, Head of IR:

Good afternoon, everyone. Thank you for joining us on the call to discuss our Q3 2021 financial results. Today we have the following speakers on the call: Deputy CEO for Commerce and Finance Andrey Chikhanchin, Deputy CEO for Strategy, Service and Marketing Andrey Panov, Director of Revenue Management and Network Planning Ivan Batanov, and myself. I would like to remind you that the press release and IFRS statements are available on our website in the Investor Relations section. The webcast presentation will be available after the call. As always, I draw your attention to the fact that some information on the call may contain forward-looking statements and actual results may differ materially from those expressed or implied in the statements made during this conference call due to known and unknown risks and uncertainties.

I would like to start with key highlights of the quarter to be discussed during the presentation. In Q3, Aeroflot Group further improved its operational and financial results despite continuous headwinds we have faced since last year's spring. This summer, we did our best to capitalise on seasonally strong quarter, with our domestic traffic up by 27% vs Q3 2019 and yields posting a 7% improvement vs Q3 2019 as well. The yield dynamics is explained by further strengthening of the international yields and slight pressure on the domestic yields. On the back of stellar performance in the quarter, the Group earned a net income of RUB 12 bn. This is the first positive quarterly result in terms of the bottom line over the last two years. This was possible thanks to exploiting all opportunities opened by the market in both domestic and international segments, as you will see later in the presentation.

Now I would like to pass the floor to Andrey Panov, who will discuss market conditions, operating performance and strategy execution.

**Andrey Panov,
Deputy CEO for
Strategy, Service
and Marketing:**

Thank you, Andrey. Hello everyone. Let me start with the overview of the Russian market, which actually feels quite good. In Q3, the recovery of the Russian market continued: the key driver was the domestic segment, which exceeded Q3 2019 results by 30% in terms of passenger traffic. The international segment, which is still under pressure from COVID-related border control measures, also posted better results, but on quarter-on-quarter basis. We transported 11.7 million international PAX in Q3, which is 2.4x more than in Q2 2021. The recovery rate stands at around 48% for Q3. The combined market volume measured in PAX amounted to 41.6 million in Q3 2021, which is 87% of the Q3 2019 PAX level. In Q2, the recovery rate was 74%, and in Q1 – 63%, so we see a great deal of progress here. The high-level picture for Aeroflot is comparable with the market. The Group has recovered 86% of its Q3 2019 traffic volume, which is an acceleration from 75% in Q2. It is worth mentioning that Russian airlines (outside of the big 4) have shown increased activity, particularly in the international charter segment that by now has almost no travel constraints compared to the European and Asian markets. It resulted in the increase of their market share, while Aeroflot Group, S7 and foreign players have marginally decreased their market share due to this structural and temporary shift.

Let us go to the next slide. As previously, monthly operating statistics provided quite an interesting visual illustration of the Russian Civil Aviation market performance (excluding foreign carriers). The recovery of the domestic segment, which started in Q1, has been remarkable. It continued throughout the year, with summer months showing a 30% growth vs the respective period of 2019. The international segment recovery rate improved from 16% in January to 42% in September (vs the respective 2019 periods). As we have mentioned above, charter carriers have been particularly active in the segment this year, as their share in international PAX in 9M 2021 amounted to 57% vs 31% in 9M 2019.

In late Q3 2021, the overall market was very close to pre-pandemic levels in terms of PAX volumes (96% for September and 98% for October).

While we acknowledge that in RPK and ASK terms the total market performance was still lagging behind pre-pandemic figures by 10–15% by the end of the quarter, which speaks to overall lower utilisation of fleet and changes in route and flight leg mixes, from the demand side the PAX traffic is probably the most relevant metric to underpin strengths of the Russian market, in our opinion.

Let us move to the next slide. Once again, we are talking about the Russian market and I can repeat my statement from three months prior – Russia is the world champion of the domestic recovery. Global domestic RPK in September is still 24% down, with PLF 9 pp below the June 2019 level. The USA, China, Brazil, Japan and Australia are also in the red territory. On the contrary, Russian domestic RPK is 30% higher, while PLF lags historical loads by only 1 pp.

When we look at the key domestic regional airports in September 2021, we see double-digit growth vs September 2019 led by popular domestic resorts. As an example, Sochi Airport in 9M served more than 9 million PAX backed by high traffic to the resort during the ski season and increased volumes for the sea cluster, as the destination offers multi-seasonal leisure opportunities.

Let us move to the next slide and talk about the Group's performance across different brands. Aeroflot Airlines posted a 37% increase in traffic compared to 9M 2020. Rossiya and Pobeda also enjoyed strong double-digit growth in the period. Dynamics by brand in 2021 on top of the recovery narrative should also be viewed with the current strategy execution in mind, as we continued to redistribute fleet and routes within the Group, which led to outperformance of LCC and regional brands compared to the flagship carrier Aeroflot. In October, we kept up our strong performance driven by LCC, which continued to expand traffic on the back of fleet growth.

On the next slide, you can see some points about Pobeda Airlines. In Q3 2021, Pobeda continued to grow fuelled by market recovery and strategic developments made during Q2, as the carrier commenced flights from the Sheremetyevo airport and replaced Aeroflot on several destinations. In summer season 2021, Pobeda operated 16 domestic and 1 international service from Sheremetyevo, including 11 routes code-shared with Aeroflot. The codeshare agreement between Aeroflot and Pobeda enables passengers to book connecting flights in Sheremetyevo, with Aeroflot servicing one leg and Pobeda another, which establishes connectivity synergies between airlines of the Group and allows companies to serve passengers more efficiently.

Thanks to the active recovery of operations in its main base in Vnukovo and rapid growth in Sheremetyevo, Pobeda added 42% more passengers in 9M 2021 vs 9M 2019, with load factors on par with the pre-pandemic level of 94%.

Here I will pass the floor to Ivan Batanov, who will do the network and schedule overview.

**Ivan Batanov,
Head of Revenue
Management:**

Thank you, Andrey. Good afternoon, everyone. Let me start by giving you more colour on Aeroflot's capacity development in Q3 and 9M 2021.

Like other market players, Aeroflot Group materially increased its domestic network, adding new flights, destinations and frequencies, and continued the recovery of its international network.

Since April, the Group has exceeded the domestic capacity of 2019 and by September operated ca. 30% more ASKs.

International capacity has also materially improved from 15% of the 2019 levels at the beginning of the year to 43% in September and 52% in October.

RPKs in the segment recovered a bit slower, creating some pressure on the system-wide load factor. This should not be seen as a challenge, as international destinations with no restrictions show healthy load factors, while destinations with restrictions on

travel (which is the main reason for load factor performance) compensate for lower load factors with better yield dynamics.

Let us move to the next slide. Following our proactive approach adopted in Q2, we continued to develop various network initiatives (both tactical and strategic) to further improve our financial results in 2021. On top of already operating cargo-passenger flights and further increasing scheduled flights to allowed CIS countries and selected European states (like Serbia, Greece, Croatia, Hungary and many others), we continued to support the following initiatives:

- Regional programme of flights from regional cities to Black Sea resorts, which covered 45 routes and had transported almost 600,000 PAX by September, helping us to utilise the fleet more intensively and rationally. The programme, though being a tactical decision, proved to be so popular with passengers that we decided to extend it to the winter schedule with a number of seasonal adjustments.
- Krasnoyarsk hub, which was launched in June 2021 with six routes connecting to business and leisure destinations domestically. This is the first step towards two-hub operations of Aeroflot, currently small in size, yet very important for the long-term development of the Group and extraction of additional synergies from regional operations.
- Regional services from a number of Russian airports to CIS countries, including Armenia, Uzbekistan and Kyrgyzstan, to leverage leisure market opportunities as well as migrant and visiting friends and relatives (VFR) flows.
- New international services to the markets open for Russian tourists, which either had not been operated before at all or not been represented on the market for a long time. These new services include flights from Moscow to Cancun, Punta Cana, Victoria and several others.

Let us move to the next slide and look at the Aeroflot Group international network.

Our initiatives in the international segment allowed us to further increase the PAX traffic recovery. It started in August 2020 with the reopening of a handful of international destinations and reached 37% of historical levels in Q3 2021.

Meaningful recovery acceleration was observed in Q3 2021 compared to Q2 2021, explained by better seasonality as well as more points served and higher frequencies to existing international destinations. Reopening of Turkey after COVID-19 restrictions and flights to Egypt materially contributed to Q3 improvement.

Growth in international PAX in 2020 and 2021 was driven mostly by point-to-point demand originating within the country, as no material number of transit passengers are travelling internationally right now, which yet again underlines the strength of the Russian consumer. Point-to-point traffic also supports international yields, which otherwise are diluted by transit fares.

Let us look at the next slide, which has Aeroflot Group scheduled revenue units.

Revenue units posted improving performance in Q3 2021 compared both to Q3 2020 and even to Q3 2019. Overall, scheduled yields are up by 24% vs Q3 2020 and 7% vs Q3 2019. As you see from the domestic and international yield analysis, this performance was mainly driven by demand-supply imbalance in the international segment – capacity materially lags the existing demand.

As expected, in Q3 the international yield commenced normalisation on the back of gradual capacity expansion (due to a very high base of Q3 2020), but remained in line with our expectations of RUB 6–7 per RPK, which is about 60% above historical levels.

The domestic segment, on the opposite, continued to be affected by high capacity operated, which explains lower yields than in Q3 2019. At the same time, we managed to improve the yields year-on-year. Despite a sizable increase in domestic capacity in Q3 2021, our pricing approach was quite consistent with a very fragile equilibrium. We consider a 5% pressure on yield to be an outstanding result in the environment of 30% growth in capacity.

Now I would like to pass the floor to Andrey Chikhanchin, Deputy CEO for Commerce and Finance, to discuss fleet and financials.

Andrey Chikhanchin,
Deputy CEO for
Commerce and Finance:

Thank you, Ivan. Hello everybody. A few words about the fleet update.

Our priority remains to avoid excessive fleet increase and ensure delivery of previously contracted aircraft only.

In the narrow-body segment, the key additions in 9M 2021 include nine A320neo family aircraft, which offer more efficiency compared to the retired A320s. In the wide-body segment, five A350 and three Boeing 777 aircraft were delivered, which resulted in gross PDP refund of RUB 27 bn in 9M. The regional segment additions are represented by six SSJs delivered to Rossiya Airlines as part of our current strategy execution. In FY2021, on a net basis we target adding twelve aircraft, focusing on regional and wide-body planes needed to support the Group's recovering network.

Financial highlights. In Q3 2021, we managed to deliver further quarter-on-quarter and year-on-year improvement across all metrics, with quarterly results moving even closer to pre-pandemic levels. EBITDA in Q3 2021 amounted to RUB 54 bn, only 26% lower compared to Q3 2019, with EBITDA margin of 32%, only 2 pp lower than in the pre-pandemic quarter. In Q3 2021, the Group delivered its first quarterly net income since the onset of the pandemic, earning RUB 12 bn, while still being ca. 20% below on revenue vs 2019. This result should not be taken for granted as it reflects the management's successful effort in changing the approach to capacity recovery: we have been proactive and focused on available opportunities on the domestic and international markets, which we discussed earlier, while ensuring tight cost control as operations recovered.

The next slide is on revenue dynamics. The Group's total revenue amounted to RUB 362 bn in 9M 2021, up 55% year-on-year, or RUB 128 bn in absolute terms. Albeit still lower compared to the pre-pandemic levels, this marks an important improvement in our quarterly dynamics, with the Q3 2021 revenue declining 21% vs Q3 2019.

The improved performance in 9M was supported by better yields, which my colleagues have already mentioned, and the currency effect. The key drivers by business segment were Russia, the CIS, American and Middle Eastern markets.

The cargo segment continued its strong performance in 9M 2021, adding about RUB 3.6 bn with strong double-digit growth in revenue in Q3 2021. Going forward, we believe our cargo revenue will normalise as more international passenger flights reopen.

Let us move to operating costs. In Q3 and 9M, the recovery was accompanied by cost control. The majority of cost lines continued to decline in double digits vs the respective period of 2019. In 9M 2021, we recorded a stronger impact from higher fuel prices. To offset the detrimental impact of growing jet fuel prices on flight economics, we are gradually introducing higher fuel surcharges across our entire network.

In 9M 2021, FX also impacted costs, but to a lower extent than usual given current limited exposure to international operations. Still, the impact was negative as the rouble lost ca. 5% of its value vs the US dollar in 9M 2021.

The increase in other expenses in 9M 2021 was mainly due to the reflection of expenses related to the Aurora codesharing in the amount of RUB 8.3 bn as a single sum in the financials, as well as the COVID-19 subsidy of RUB 8 bn reflected in 9M 2020.

Next slide – the Group's unit costs. As we further recover operations and utilise higher capacity volume, we see improving CASK dynamics. It is still elevated over the RUB 3.1

normalised level of Q3 2019 as it is distributed between fewer ASKs. However, it is a sizable improvement compared to previous quarters.

Fuel cost management. As mentioned earlier, we continue to see pressure from jet fuel, recording a consecutive increase in the jet fuel price since May 2020. In Q3, we crossed the pre-pandemic threshold as the jet fuel price in July 2021 moved above July 2019. Aeroflot continues to enjoy flexibility in jet fuel pricing thanks to contract structures, under which we currently have a longer lag before higher oil prices transform into higher prices for jet fuel.

Also, we take hold of reduced timing for forward bookings, which supports efficient cost planning. At the same time, we recently introduced higher fuel surcharges to compensate for current jet fuel dynamics.

In addition, some help comes from the damper mechanism, which allows for receiving compensation for 65% of domestic fuel supplies if the price is over a certain officially set threshold.

Let us move to the next slide, Pobeda financial results. Despite the extremely complicated situation in the industry, Pobeda continued to grow its business in line with the existing strategy. In 9M 2021, its revenue amounted to RUB 53 bn, growing 85% year-on-year on the back of PAX traffic growth, yield and load factor improvement. Thanks to continuous focus on cost control, OPEX increased only by 75%, which allowed us to realise positive operating leverage and improve operating income, achieving operating margin of 18%. Bottom line also showed significant improvement year-on-year, with net income amounting to RUB 6 bn in 9M 2021.

The next and last slide has to do with leverage and liquidity. As of the end of Q3, the Group's cash position remained strong, amounting to RUB 93 bn. This was helped by extra liquidity coming from PDP reimbursement as total net refunded PDP amounted to RUB 5.5 bn in Q3 2021. A decline in cash of ca. RUB 20 bn vs June 2021 was seasonal, associated with the fulfilment of obligations to passengers as a result of traffic recovery in Q3 with a subsequent seasonal slowdown in the number of future bookings.

Total debt did not increase materially during the quarter as borrowings and lease liabilities stayed flat. As we further recover operations and grow EBITDA, Net Debt to EBITDA ratio normalises. The Group's debt structure is sitting comfortably at 18%/82% short-term/long-term borrowings shares as at 30 September 2021.

Overall, Q3 has been quite successful from the cash generation perspective, and we stepped into seasonally lower quarters with ample liquidity necessary to cross over to the next high season.

That is all for the presentation, and we are ready go to the Q&A session. Thank you.

Q&A

Matvey Tayts, Sovo Capital:

Good afternoon, thank you for this presentation. The main question for me is how you see the international yields performing going forward this year. Do you see them normalising more rapidly or going much higher than it was in 2019? This is my first question. A couple more. How much did you receive as a compensation for this very high fuel price, if you can indicate a particular number? What is the average volume you will receive monthly, assuming the current level of the oil prices? If you may indicate that. Also, I have a question about your strategy execution. You continue to transfer aircraft from Aeroflot Group to Pobeda. What is your plan until the year-end? How many jets will you transfer? What is your plan for the next year? Thank you.

Ivan Batanov, Head of Revenue Management:

Let me start with the first question. As already mentioned, the international yields are higher than before. Taking the actual figures, we forecast for Q4 yields of RUB 5–6. However, I need to stress that we continue to reopen the international network, and around 50% in terms of passengers has been recovered. As we go further, the yields will normalise. But it is still difficult to provide timings, as they depends on the reopening.

Andrey Chikhanchin, Deputy CEO for Commerce and Finance:

OK, Matvey, can we go to the next question about the damper?

Matvey Tayts, Sovo Capital:

Yes.

Andrey Chikhanchin, Deputy CEO for Commerce and Finance:

According to the 9M statement, there was a non-material sum of about RUB 65 mn for Aeroflot and about RUB 100 mn for the Group, but the figures for the following months became bigger. We think the compensation for Q4 should amount to more than RUB 1 bn. I think so.

Matvey Tayts, Sovo Capital:

Thank you. And about your strategy?

Andrey Panov, Deputy CEO for Strategy, Service and Marketing:

Regarding the last question about transferring our fleet to Pobeda, the initial plan was to transfer approximately 50 Boeing 737s to Pobeda. We have already transferred ten of them, and this year we will not transfer more. The remaining 40 planes will be transferred in two years, approximately 20 per year. There can be some small changes, but this is the plan.

Matvey Tayts, Sovo Capital:

Thank you very much.

Ivan Postevoy, VTB Capital:

Good afternoon, everyone. Thank you for your presentation. I have several questions. The first one is to complete the picture on yields. Could you please provide your

expectations for the domestic yields in Q4? The second question is a bit philosophical – are you ready for jet fuel prices to remain at current levels in 2022? And the third question. What cash burn do you expect in Q4?

**Ivan Batanov,
Head of Revenue
Management:**

Let me start with the first question. With regard to the domestic yields, I would like to highlight that October was very much positive for us. With quite a high load factor, the decrease in yields was less than we expected. I would suggest forecasting Q4 domestic yields based on the seasonal decreasing trend that we saw in Q3.

**Andrey Chikhanchin,
Deputy CEO for
Commerce and Finance:**

As for the next question on 2022 jet fuel prices, you have to understand that the price is not dependent on us. Right now, we do not see any positive factors or information to indicate that the price would go extremely down. Still, we expect some decline in the price according to what oil market experts are saying. But if the price remains largely the same, we will accommodate that, we will not just stop because of that, of course.

As for cash burn, according to our figures in October and November we burnt about RUB 10 bn. In December, we will try to minimise this figure, but everything will depend on forward bookings. However, the figures should not exceed those that I mentioned earlier.

**Ivan Postevoy,
VTB Capital:**

Just to clarify, is it RUB 10 bn for two months or for each month?

**Andrey Chikhanchin,
Deputy CEO for
Commerce and Finance:**

It is a combined figure.

**Ivan Postevoy,
VTB Capital:**

Okay. Thank you very much.

Operator:

We have a follow-up question from Matvey Tayts, Sova Capital. Please go ahead.

**Matvey Tayts,
Sova Capital:**

Yes, thank you. My question is about the potential introduction of QR codes for flying. Have you conducted any studies? What percentage of your passenger flow already have this QR code that will potentially be necessary for flying? How do you estimate the impact of this potential measure? What is the right way to look at it? Your view would be really helpful. Another question is about the holiday season ahead. December has almost come. What does it look like compared to previous years? What is your estimate on this New Year's travel season? Thank you.

**Andrey Napolnov,
Head of IR:**

Matvey, thank you for your question. It is a very difficult one. Unfortunately, we do not have any study data in this field now. If you travel internationally, you need to pass a PCR test. In several countries, the Sputnik V vaccine is accepted. So checking some kind of travel medical document for international travel is a reality for over a year now.

However, for all destinations in our network, for domestic segment, we so far do not have this information based on research and would like to avoid sharing assumptions. We believe that if and when this legislation is introduced, continuous progress in vaccination is important, and we see it happening right now. Also, I would like to say that, again, if the respective law is passed, Aeroflot will be ready IT-wise. This is what we can say on this point.

**Ivan Batanov,
Head of Revenue
Management:**

Let me answer your second question. If we look at the New Year's holidays, the trends are usual for this time of the year. Internationally, we can see strong results – there is additional demand coming from new long-haul flights to the Caribbean. As you know, we are reopening Thailand. Recently, the flights to Egypt, the Maldives, the Seychelles have reopened and now are even more popular than the available European destinations, which is normal since these destinations are almost fully open for Russian tourists. All these flights will support us in a big way in the coming holiday season. In Russia, there is currently an elevated demand for resort destinations, with Sochi being one of the most popular destinations. As usual, our revenue management is based on demand – the demand is high, and it is reflected in pricing.

**Matvey Tayts, Sova
Capital:**

Thank you. If I may, one more question about the domestic market. We saw a rapid growth in domestic flights this year. What is your estimate regarding domestic flights growth for the next year? Is it already saturated or will it continue growing? Thank you.

**Andrey Panov,
Deputy CEO for
Strategy, Service and
Marketing:**

Let me answer. Let us speak about it not only in terms of the next year, but the next few years. We believe that the high growth that we observed this year will not be the same in the following years, and we will return to a normal growth trajectory. It depends on the overall situation around COVID-19 and borders, etc. In general, we do not expect a second year of “super growth.”

**Matvey Tayts, Sova
Capital:**

Okay. Thank you very much.

**Andrey Napolnov,
Head of IR:**

Thank you everyone for participating in the call. If you have any follow-up questions or need any clarification on reported results or statements made during the call, we will be happy to discuss them after we finish this call. Thanks a lot and goodbye.

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KEY UPCOMING EVENTS

FINANCIAL CALENDAR

December 2021	Aeroflot Group November and 11M 2021 traffic results
January 2022	Aeroflot Group December and FY 2021 traffic results
February 2022	PJSC Aeroflot FY 2021 RAS results disclosure (standalone)
February 2022	Aeroflot Group January 2022 traffic results
March 2022	Aeroflot Group FY 2021 IFRS results disclosure (consolidated)
March 2022	Aeroflot Group February and 2M 2022 traffic results