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Surf Air Mobility, Inc. (SRFM)

Q2 2024 Earnings Call

CORPORATE PARTICIPANTS

Deanna White

Interim Chief Executive Officer & Chief Operating Officer, Surf Air Mobility, Inc.

Oliver Reeves

Chief Financial Officer, Surf Air Mobility, Inc.

OTHER PARTICIPANTS

Austin Moeller

Analyst, Canaccord Genuity LLC

MANAGEMENT DISCUSSION SECTION

Operator: Thank you for standing by. At this time, I would like to welcome everyone to today's Surf Air Mobility Second Quarter 2024 Earnings 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. [Operator Instructions] Thank you.

I would now like to turn the call over to [ph] Sam Levinson. Sam (00:27), please go ahead.

Unverified Participant

Thank you, operator. Welcome to Surf Air Mobility's second quarter 2024 earnings call. I'm joined today by Deanna White, Chief Operating Officer and Interim Chief Executive Officer; and Oliver Reeves, Chief Financial Officer. Our earnings results can be found on the SEC EDGAR website and on our Surf Air Mobility Investor Relations page at investors.surfair.com.

During this call, we will discuss our outlook and expectations for future performance. These forward-looking statements may be preceded by words such as we expect, we believe, we anticipate or other similar statements. These statements are subject to risks and uncertainties, and our actual results could differ materially from those views expressed today. Some of these risks have been set forth in our earnings release and in our periodic reports filed with the SEC.

During today's call, we will present both GAAP and non-GAAP measures. Additional disclosures regarding non-GAAP measures, including a reconciliation of GAAP to non-GAAP measures, are included in the earnings release we issued earlier today posted on the Surf Air Mobility Investor Relations website and in our filings with the SEC.

I'll now turn the call over to Surf Air Mobility's Interim CEO, Deanna White. Deanna?

Deanna White

Interim Chief Executive Officer & Chief Operating Officer, Surf Air Mobility, Inc.

Thank you, [ph] Sam (01:47). I would like to welcome everyone who has joined our call this evening. As many of you know, I have been with Surf Air Mobility since 2021 and previously served as a Chief Financial Officer. Approximately 90 days ago, I became the Chief Operating Officer and Interim Chief Executive Officer. I know the organization well and understand our opportunities to lead innovation in our industry. I'm excited to be here to execute our strategy.

Let me start by noting how pleased we are with the financial results of the second quarter. Revenue for the quarter exceeded our expectations and rose over 13% year-over-year on a pro forma basis. Adjusted EBITDA results were materially better than our expectations, with an adjusted EBITDA loss of \$11.8 million as compared with our expectations of a loss of \$16 million to \$18 million.

Let me take a moment to address the important announcement we made yesterday related to our new venture with Palantir Technologies. We have been working with Palantir since 2021 to develop and deploy software and analytical tools across all three of our air travel brands. Going forward, we will form a new venture with Palantir, Surf Air Technologies LLC to further develop market and sell a software platform solution for the advanced air mobility industry.

At the center of this solution sits SurfOS, a category-defining operating system and an all-in-one holistic suite of software tools to enable operators to more efficiently run their businesses. Components will include flight distribution, airline and charter operations, revenue and demand management, business intelligence, financial reporting, and customer service. Surf Air Mobility will become the first customer of Surf Air Technologies and will thereafter leverage Palantir's sales force to offer SurfOS to Part 135 operators, existing aircraft manufacturers, and manufacturers of clean-sheet design electric aircraft.

Surf Air Technologies has unique relationship with Palantir, designed to penetrate the Part 135 market and harness the growth of the emerging regional air mobility segment of the aviation industry, which McKinsey estimate at between \$75 billion and \$115 billion by 2035. Using Palantir tools and processes, we will advance our efficiency, innovation, and leadership position. An important reason for the formation of Surf Air technologies is to sub-capitalize or [indiscernible] (05:03) finance our software platform and reduce the capital burden on Surf Air Mobility.

During the second quarter, we made significant strides in the development of our software, adding exciting new features to our platform. First, we layered a Palantir-powered solution into our new Pilot check-in mobile app, which validates a pilot's eligibility before he or she takes a flight.

Second, we started training a large language model, Ask Sam, on operational documentation such as aircraft manual and operating specs, pilot training manuals, and flight logs to serve our future AI needs.

Third, we worked on digitizing flight log records. Today, one of our pilots can take a picture of a handwritten flight log into our mobile app, which will automatically digitize it, store it, and allow someone to make [ph] prompts (06:03) against the data using OpenAI's engine via Palantir. These features are just a small example of how software solutions and AI applications can meet the needs of our industry, which will only become more complex as the industry matures and expands.

Turning to our electrification initiatives, our aircraft electrification program remains on track to complete the conceptual design phase by the end of the fourth quarter of 2024. At that stage, we will have selected the key supplier for the electric EP1 variant and will have concluded commercial agreements with our core supplier group.

Regarding the hybrid EP1 variant, we have made significant progress on the preliminary design, having completed a series of trade studies. We are now confident in the system's performance and viability and the capacity of the supply chain to support its commercialization.

With regard to our STC, we remain on track to meet our 2027 deadline. We intend to take a similar approach with our electrification initiative as we have with our software and technology initiative, partnering with leading electrification supply chain partners to create a venture focused on building electrified powertrains for the Cessna Caravan and thereafter other turbo aircraft. As with our software platform initiatives, we intend to pursue the sub-capitalization of our electrification initiative.

Now, turning to our mobility initiative, in the last three months, we have moved rapidly to effect change and reposition our regional airline operations for success. First, we have augmented our leadership team. In June, we named Jim Sullivan President of Air Mobility. Jim is an airline industry veteran with experience as CEO and COO of a Canadian airline and his previous experience as a commercial pilot and VP of flight operations at both JetBlue and Frontier. Jim is overseeing our regional airline operations and commercial strategy across all three of our travel brands.

In July, we named Louis Saint-Cyr President of our Hawaiian operations, reporting to Jim. Louis previously served in operations and guest experience roles at Hawaiian Airlines, Air Canada, and WestJet. Jim and Louis have joined me to bring new focus and rigor to our regional airline operations and as the second quarter results show, we are [ph] notching (09:02) many early wins. Our regional airline operations, previously known as Southern Airways, produced positive adjusted EBITDA for the second quarter, which reversed a long-standing trend.

An early focus of the new team was to examine the profitability of each of our scheduled routes. This analysis identified unprofitable routes we have begun to discontinue. As mentioned last quarter, we added two new routes between Purdue University and O'Hare and between Williamsport, Pennsylvania and [ph] Dallas (09:41).

Next, we are focused on our essential air service routes, which currently serve 20 markets and the anticipated positive impact from the passage of the FAA Reauthorization Act, which raises the cap on subsidies. The raised cap will potentially make existing routes more profitable when they are rebid and open new markets that would be attractive for us to bid on.

Third, we are implementing new systems, processes, and workflows coupled with real-time operational and financial KPI to accurately measure performance against aviation standards. We are developing a best-in-class operation center, network of maintenance facilities and stations to more effectively support our geographic footprint.

Fourth, we are applying rigor to identify new growth markets for scheduled services and mapping out the timing of our needed equipment. We will be taking delivery of eight new Caravan aircraft in the third and fourth quarters of this year. These initial deliveries will replace aging equipment and will have an immediate positive impact on fleet availability and completion rates, which in turn will drive increased revenue and maintenance cost reductions.

Going forward, we are optimizing the quantity and timing of new aircraft deliveries to most effectively deploy new aircraft to growth markets, further expanding our leadership position as the largest commuter airline in the US by departures. To put it simply, our first priority is improving our existing operations and our second priority is ensuring that we enter new markets profitably.

Last is important to understand that we work today with over 15% of the Part 135 operators in North America booking charter flights. These operators are vendors to us today and will be our customers tomorrow for our SurfOS software platform and our electrification products. As evidenced by the revenue growth we have achieved in On Demand services, our distribution platform continues to expand, further enhancing the network effect in our business model.

To govern the transformation of Surf Air Mobility, I have implemented a strategic process across people, process, and technology, which is serving as our road map for change. I look forward to discussing these pillars with you in more detail when we host our Investor Day in a few months. At that time, we will also discuss the early signs of progress from the work we have done as well as our revised go-forward strategy.

Now, let me take a moment to summarize what I have shared with you. We are moving fast. We are repositioning our strategy to drive profitability, reduce our capital needs, and expand our industry leadership. We are partnering with exceptional companies such as Palantir and Textron to leverage our joint capabilities and further distance ourselves from the competition. We have new leadership, new systems, processes, and workflows, and a new strategic road map that we are executing against. We are [ph] notching (13:18) early wins. We have a commitment to success and we look forward to keeping you informed of our progress over the coming quarters.

With that, I will now turn the call over to Oliver to discuss our Q2 results and our outlook for the third quarter. Oliver?

Oliver Reeves

Chief Financial Officer, Surf Air Mobility, Inc.

Thank you, Deanna. Revenue in the second quarter of 2024 rose 13.2% over the prior year period on a pro forma basis to \$32.4 million, exceeding our expectations of \$28 million to \$31 million. This double-digit revenue growth was driven by 13.8% growth in Scheduled service revenue and 11.7% growth in On Demand service revenue. The increase in Scheduled service revenue was primarily driven by the launch of subsidized flight operations on the Lanai route in Hawaii and the Purdue and Williamsport routes. The increase in On Demand service revenue was driven by a 13.1% increase in departures over the comparable period.

As Deanna mentioned in her comments and as we discussed on our call last quarter, we undertook an analysis of all of our scheduled routes and have taken steps to either discontinue or improve the profitability of underperforming routes. Overall, increased subsidies and necessary cost cuts contributed to our improved profitability. As a result, our regional airline operations produced positive adjusted EBITDA for the second quarter. Importantly, this did not come at the expense of revenue growth and as expected, does not yet reflect any positive impact from the FAA Reauthorization Act.

On a pro forma basis, adjusted EBITDA loss increased modestly year-over-year to \$11.8 million from \$11.1 million. We are very pleased with this outcome as it is materially better than our expectations of an adjusted EBITDA loss of between \$16 million and \$18 million for the quarter. Renewed vigor on cost control implemented by the new management team is already beginning to show results and we are now targeting positive adjusted EBITDA at our regional airline operations for the full fiscal year.

Turning to liquidity, as of June 30, 2024, Surf Air Mobility had \$1.5 million of cash on hand, with the ability to draw \$90 million in committed draws and up to \$296 million in follow-on draws subject to the terms of the GEM share subscription facility. As a reminder, we continue to purposefully manage our cash balance to minimize the utilization of the GEM facility.

Recently, we closed on our previously announced \$35.2 million convertible security with GEM Global High Yield (sic) [GEM Global Yield] (15:52). The new security cancels a significant portion of GEM's currently issued and freely tradable shares in the company. It imposes a volume restriction on daily trading and gives us the flexibility to redeem all or part of the security in cash at 115% of the then outstanding par amount. Importantly, as Deanna mentioned, we have agreed to form Surf Air Technologies, a venture with Palantir. And we will be working together with them to bring in outside investment to sub-capitalize and fund our SurfOS software initiative and thereby reduce the spend from Surf Air Mobility.

Now, turning to our guidance for the third quarter, we expect third quarter 2024 revenue in the range of \$25 million to \$28 million, pro forma adjusted EBITDA loss in the range of \$10 million to \$13 million, which excludes the expected impact of stock-based compensation, changes in fair value of financial instruments, and other non-recurring items. The company's expectations for the third quarter reflect the impact of unplanned maintenance of aircraft over the last two months, resulting in lower [ph] completion (16:56) factors.

Due to these factors, the company currently expects that its regional airline operations will be marginally unprofitable on an adjusted EBITDA basis in the third quarter. Importantly, the company continues to execute a series of actions to improve profitability and is targeting profitable regional airline operations for the full year.

With that, let me turn the call back over to Deanna for some closing thoughts.

Deanna White

Interim Chief Executive Officer & Chief Operating Officer, Surf Air Mobility, Inc.

Thank you, Oliver. In my new capacity as Chief Operating Officer and Interim CEO, I would like to take a moment to share with you why I'm so excited about the opportunities ahead for this company. We are the largest commuter airline operator in the US and we are advancing the very notion of air mobility. We operate in a vast marketplace ripe for disruption. By partnering with Palantir, Textron, and other leading organizations, we are bringing new innovations to the market.

We are pioneering the path into fertile territory, empowering our operations to capture market growth, drive efficiencies and profitability, and expand our offering across air mobility networks worldwide. We are still in very early innings, but we cannot be more excited about what lies ahead and we look forward to keeping you apprised of our progress.

I would like to thank everyone who has been with us on this call today. I will now turn the call over to our operator so that we may take some of your questions.

QUESTION AND ANSWER SECTION

Operator: Thanks, Deanna. [Operator Instructions] And while we're waiting, just want to remind you again, joining us today to answer your questions are Deanna White, Chief Operating Officer and Interim CEO; Oliver Reed (sic) [Reeves] (19:01), Chief Financial Officer; Sudhin Shahani, Co-Founder of Surf Air Mobility; and Ido Gruberger, Chief Strategy Officer.

And it looks like our first question today comes from the line of Austin Moeller with Canaccord Genuity. Austin, please go ahead.

Austin Moeller

Analyst, Canaccord Genuity LLC

Q

Hi. Good afternoon. Just my first question here. What was the passenger load factor on the Purdue and Williamsport routes currently and how many flights do you [Technical Difficulty] (19:30) per week?

Deanna White

Interim Chief Executive Officer & Chief Operating Officer, Surf Air Mobility, Inc.

A

This is Deanna. Thank you for your question. You broke up a little bit. It was hard to hear the second part of it, but you were talking about the load factors on our newly launched Purdue and Williamsport routes. The load factors are in the 50% approximately and improving. And both of those routes has shown us to be profitable for the time we've operated them right out of the gate with the private subsidies we have with those two partnerships.

Austin Moeller

Analyst, Canaccord Genuity LLC

Q

[Technical Difficulty] (20:10).

Operator: Austin, we're having a hard time hearing you.

Austin Moeller

Analyst, Canaccord Genuity LLC

Q

Can you hear me now?

Operator: A little better. Go ahead.

Austin Moeller

Analyst, Canaccord Genuity LLC

Q

[Technical Difficulty] (20:30) flights you have scheduled on those routes per week?

Deanna White

Interim Chief Executive Officer & Chief Operating Officer, Surf Air Mobility, Inc.

A

Austin, this is Deanna. I think you said how many flights do we have scheduled on each one of those routes per week. I don't have those exact numbers with me but I can get back with you and circle back with an answer after the call.

Austin Moeller

Analyst, Canaccord Genuity LLC



Okay, great. Thanks for the details.

Operator: All right. Thank you, Austin. And ladies and gentlemen, that does conclude our prepared remarks today. Thank you so much for joining and you may now disconnect. Have a good day, everyone.

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