

Q1 2022 Earnings Call

Company Participants

- Caio Goncalves Moraes, CFO
- Helium Rotenberg, CEO
- Renata Battiferro, IR

Other Participants

- Bernardo Guttman, Analyst
- Unidentified Participant, Analyst

Presentation

Renata Battiferro {BIO 19330325 <GO>}

(Technical difficulty) And it's a privilege to be here with you.

Joining us today, Mr. Helium Rotenberg, company's CEO; and Caio Goncalves Moraes, CFO and Director of Investor Relations.

We'd like to inform you that this video conference is being recorded and it will be made available on company's IR, where the slide deck is also available. (Operator Instructions)

We'd like to emphasize that information contained in this presentation and any statements that may be made during the video conference concerning the company's business prospects, projections and operating and financial targets are based on management's beliefs and assumptions as well as on information currently available.

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Investors should understand that general economic conditions, market conditions and other operating factors may affect the company's future performance and lead to results that differ materially from those expressed in such forward-looking statements.

Now I'd like to turn it over to Helium, so that he can start the presentation.

Helium Rotenberg

Good morning, good morning, everyone. We are going to share our results that we find to be very good, and based on the planning that we conducted back in 2018, and it proves that we are on the right way.

Our gross revenue is BRL 1.2 billion, so almost 50% more than last year, so year-over-year. And why do I say that we really got it right by betting on diversification? Because when one segment is not providing good results, another one is achieving the results we wanted. And that's why we are now balanced. We have a very diversified portfolio, and we operate in different segments. That certainly strengthens our company, and it ensures sustainable growth over time.

The EBITDA was BRL 126 million in the quarter, LTM EBITDA of BRL 409 million, historical record. Also adjusted net income of BRL 28 million this quarter, and we are going to also go in depth in these numbers. As for the portfolio mix, it's very, very important because it transcends in other segments, except for the consumer unit. So when consumer spending is not doing good and what we see today and since last October is that the entire retail market is really suffering, is having challenges.

So that's why we see this drop in consumer spending, but we see a strong increase in corporate business and also public institutions that are public organizations. With such robust portfolio for corporations, they start with desktop PCs, notebooks, to parts, services, this portfolio makes sense to small, midsized and large companies as well as to all public organizations. Besides that, we are strengthening our service units, also and tech services. And with that, we achieved a growth of 276%.

As for dividends, BRL 47.5 million or BRL 0.34 per common share. As for the pandemic, we had faced many issues in August, but now we are doing much better. So -- this is actually regarding the challenge we faced the supply chain. We still see some disruption, particularly with the lockdown in China. So we see many products being held at Panama Canal. So it takes a little bit longer. Freight is more expensive. But we still are able to carry on with our activities. So we are facing some issues with components, but we are being able to overcome them. So we still face some challenges, but not as much as we had in the past.

Next slide, please. This is a portrait of what I mentioned about diversification. You can see the chart, and we can see how much it has changed. So consumer spending is low, accounting for only 13%, corporate 28%, and public institutions 59%.

Let me first address corporate segment. We see strong demand for PCs, now that companies are resuming in-person work. In the past people were working from home, but now this scenario is changing and we see there's a strong demand for computers, especially in every single segment, small, midsized and large companies. We also see some large projects. The market now is looking for this type of service, and they are coming to us.

As for payment solutions, we still did not achieve our potential, but we are growing and we expect to see an increase in payment solutions. As for public institutions, part of this

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60% are from the ballot boxes, and that certainly makes a difference. We are going to deliver more electronic ballots this quarter, mostly in the second quarter, and we have also won another bid of ballot boxes starting 2023. And we are also -- we have also a strong share at the Secretariat of Education in different states. So it's very, very important that every student has a laptop in their hands.

Now let me talk about consumer segment. It's not that we had a significant drop, but sellout that accounts for the market presented a 10% to 15% decrease. The same for smartphones. So starting last September, we started to see this decrease. But retailers expected higher revenues. They sold 80% to 87%. And with that, their inventory level was high at the turn of the year. With that, they did not buy. There was no selling. Although the results from the first quarter of 2022 was much better than last year.

Last year, we had a 15% drop; this year, 10%, 11%. But that did not improve selling because retailers, in general, had a good inventory level. And as we all know, this drop is not only in laptops and smartphones, it's a generalized drop. We are facing now high inflation rates, high borrowing rates, loaning rates, and that's why we expect to see better selling in the second quarter of 2022, not as high as we had last year, but we expect to see consumer segment increasing in the second quarter. And for public institutions, our share is strong and expect to keep it like that.

Now let's talk about our financial highlights. I will turn it over to Caio, our CFO and Director of Investor Relations, so that Caio can go over these numbers.

Caio Goncalves Moraes {BIO 18682110 <GO>}

Thank very much,. I think Helium has already provided a very good summary of what happened. Starting with the revenue, we can see that we achieved the record gross revenue. And let me remind you that first quarter is usually the weakest one we have. But you can see that we are only 5% -- we achieved the number that's only 5% less than last quarter of 2021. So that really proves the strong demand from corporate segments and public institutions. Once again, just stressing the importance and how right we were with our diversification strategy.

Now let me talk about EBITDA. As for recurring EBITDA and EBITDA margin, as you can see, we achieved also a record BRL 126 million as well as for the last 12 months. EBITDA reflects also the diversification of revenues with increase in our growth avenues that bring better margins such as services in general, not to mention leverage coming from other activities that we have implemented -- we had an increase in our general costs that certainly reflected the growth of our company, but they increased less than our growth in revenue. So we have a better product mix and also decrease in our general costs, and that improved our EBITDA margin.

Next slide, next 2 slides. Let's talk about our net income. It's very important to understand what happened over the 2 quarters. So this reconciliation starts from the net income of the first quarter in 2021. And we are comparing these numbers. So we make an

adjustment regarding hedgings from beginning of 2021. That means that in our quarterly results, we have only what was liquidated for that specific quarter.

So we generate a better EBITDA of BRL 73 million. So a very strong operating margin. But that is loses -- we have a decrease in that number because of the currency exchange rate. We see really a major difference. But also when we think about the first quarter of 2022, we had a decrease in the currency exchange rate, i.e. the U.S. dollar. And we also had the investment that was done.

So we know that with the growth of the company, we also need to increase our inventory levels. And what you see is our net income, BRL 28 million. And we believe that this is an isolated number considering sales in the first quarter. First quarter of the year is usually the one in which we sell less and considering also the future with continuous diversification of revenues.

Our inventory levels also reflect that. If we go over our current inventory, we have approximately BRL 3 million, which is certainly achievable if we follow our guidance that is being reaffirmed. That means that we'll have more -- another BRL 4 billion to deliver, and with the decrease of inventory levels, with improvement in retail segment and increasing other segments.

Now considering the future and the delivery of ballot boxes, not to mention some other large corporate and government projects, we will generate more cash, increase our EBITDA. And that certainly allows us to feel very comfortable with our net income. So we believe that this level of net income will actually increase in the next months because of the reasons I have already mentioned. So we have already talked about net income. This is just the historical numbers quarter after quarter.

So if we move to Slide 9 to talk about ROIC. So as we mentioned, return on the capital invested is based on our future projects. And in spite of that, we see an increase in our operating income. So you see that we expect to see also an improvement in our ROIC. As for that, although you can see that the number has increased and especially to fund working capital, I'd say that that has a very good quality. We have 50% of the long-term debt that is rising the capital market.

Now I'd like to turn it over to Helium again, so that he can give us his final remarks.

Helium Rotenberg

So our estimate of a company's gross revenue for 2022 is between BRL 5 billion and BRL 6 billion, and we feel very comfortable because we have already achieved BRL 3.9 billion coming from the ballot boxes and rest of that amount coming from also government contracts. We also have a strong delivery for Petrobras. We will deliver the largest server in Latin America.

This server ranks 25. It is a project that we have been partnering with [Actos]. And also, as for Payment Solutions, we are very also -- we believe in the growth of payment solutions,

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both Cielo and Stone, and we already have agreement signed with them, and we expect to sign some others agreements, we have already signed many contracts this year. And we see also -- we expect to see growth in this segment.

And also services, tax services does not represent a large share yet, but we also expect to see good results. As for retail, although we see this downturn, we also expect reasonable results. Because of Infinix, Infinix started to be delivered at stores at the beginning of May. So we will start to see sales now in May. We ran a pilot project last will really see the actual results. So products, smartphones ranging from BRL 1,500 to BRL 3,000.

So I'd say that we really have a great strategy, and that started once again back in 2018. That certainly reflects the good results, good results income, and that's what we expect for next year. We are very optimistic.

Thank you very much, and now we open for questions.

Questions And Answers

A - Renata Battiferro {BIO 19330325 <GO>}

(Operator Instructions) Bernardo Guttmann from XP.

Q - Bernardo Guttmann {BIO 22426541 <GO>}

I actually have two questions. First one is about consumer segment. I think that Helium and Caio provided us a very good explanations about this downturn in this segment. But I'd like to -- can you please elaborate on the inventory levels in retail? And what can you expect regarding consumer segment for the rest of this year?

Second question, IoT, so smart homes. Can you please give us some color talking about company's future initiatives to expand your presence, perhaps expanding our portal or by creating a network of dealers? Or if you are going to keep working on the do-by-yourself model? So these are my two questions.

A - Helium Rotenberg

Your second question is really a provocation. So let me start with your first question. With regard to retail, we expect to see an improvement. Sell-out presented a decrease starting September of 2021, and that happened to entire retail and all types of goods. It was not different for us. But that decrease led to high inventory levels at the turn of the, and that happened to us as well because retailers did not buy as much as we had expected.

First quarter was the quarter in which the retail achieved some balance, not achieving the levels of last year, I'd say 10% less, and we expect to have that around that number. Specialists actually stated that this year we will see 10% less volume compared to 2021, which is what we are experiencing right now.

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So retailers not buy in the first quarter, and that's why our inventory levels are higher in the first quarter regarding components and products to consumers. But now in April and May, we already see larger orders. So our inventory levels should achieve a balance in July. July, beginning of August, we believe we will achieve our regular levels for retail, and they are not really high.

We really had high inventory levels regarding what we need to deliver to government and corporate in the second half, particularly electronic ballots. So we now have inventory of components for electronic ballots. But we expect also to see a normalization of those levels in the third quarter of 2022. So that's my answer regarding inventory.

As for your second question, this is certainly our major challenge. As you well said, we entered the segment by do-it-yourself. So retail and do-it-yourself. And although we see an increase in the segment, we also have a very fierce competition. There are no entry barriers, much less than what's expected. So we have many companies that actually provide light bulbs. Our share is close to 50%.

But inspite of that, we don't see the proper, consistent revenue. So we are expanding our portfolio. We will have lots of robots, an entire line of routers. We will also introduce a new comprehensive lighting system. But we don't expect to see a significant increase in our revenue coming from this segment. For achieving that, we would have to enter the do-it-for-me with the network of integrators, and we are strongly inclined to start to that. We are now taking the first steps for doing that.

A - Renata Battiferro {BIO 19330325 <GO>}

Our next question comes from [Mr. Peter Oliver]. He asks, what's the impact of the increase of interest on the company? Funding is increasing, working capital with high rates. What about your net margin? Can we expect the same level of net margin that you achieved in 2021, which was 6%, positive 6%? Caio.

A - Caio Goncalves Moraes {BIO 18682110 <GO>}

Thank you, Peter, for your question. In our presentation, we addressed the impact BRL 34 million, as I mentioned, but we have also explained that this first quarter of the year is the weakest one in results. And secondly, this impact is for our working capital because we are increasing as a company. If you think about 2 years ago, our revenue was BRL 2 billion. And last year, we achieved EUR 4 billion. Our guidance is to achieve BRL 5 billion to BRL 6 billion this year.

Obviously, we need them to finance our working capital, but with these large projects, the ballot boxes and the Petrobras project, large corporate and government projects. For the second half of this year, we may be able to decrease these investments with -- regarding working capital. So we may decrease this expense with interest. So your question about achieving the same less margin, yes, we even surpass that number.

A - Renata Battiferro {BIO 19330325 <GO>}

(Operator Instructions).

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A - Helium Rotenberg

Few questions today.

A - Renata Battiferro {BIO 19330325 <GO>}

Yes, if there are -- I really wish we had more questions. Let me see. Yes, I think we got more questions. We have a question from Guilherme Rasa [ph] from Sala Invest [ph].

Q - Unidentified Participant

Kudos for your results. Now I'd like to know about the EBITDA margin, recurrent EBITDA margin delivered by the company.

A - Helium Rotenberg

Caio, can you please answer that question?

A - Caio Goncalves Moraes {BIO 18682110 <GO>}

Thank you for your question, Guilherme. Our EBITDA margin has increased. Two years ago, it was 6% to 7%. We achieved 10% at the end of 2021, and we have been keeping that level. So in this first quarter, the number was 12%. So your question is, are we going to keep this level? We believe that we can certainly achieve 10% to 12% through 2022 with the new projects, our growth avenues.

So we see an increase in services, payment solutions, all of them delivered better EBITDA than our core business. Although we see this decrease in consumer segment and laptops, we are still able to keep this margin. So this recurrent margin that we saw last year and that we also achieved this year may be achieved over 2022 to around 10% to 12%.

A - Renata Battiferro {BIO 19330325 <GO>}

We have another question from Victor Lopez [ph].

Q - Unidentified Participant

Should we expect a variation in your mix of payment solutions according to seasonality? And what about your share coming from public institutions? Will it drop in 2022?

A - Helium Rotenberg

Victor, we believe that consumer spending will increase. We are sure that we will see an increase. But government institutions share will also remain strong, as I mentioned, BRL 3 billion, considering the ballot boxes and other public organizations. And this is for 2022. So if it's a decrease in the first quarter, we will still see a strong revenue coming from the government, particularly ballot boxes in just other quarters.

A - Renata Battiferro {BIO 19330325 <GO>}

Thank you for your question. Now we have another question from [Mr. Peter Libero]. What about the pipeline of your contracts with the government? Are you winning other bids?

A - Helium Rotenberg

Yes. Today, it's approximately BRL 3 billion. And this is what has already been signed. But we are working on that. There is a pipeline of future requests for proposals that we'll achieve BRL 7 billion. So we expect to sell tablets, notebooks. The Ministry of economy also has a bid for desktops and laptops. So there are many large projects, and we expect to see this -- maintain this growth. And also, we had to hold back some projects because we do not have enough components. But for -- in the fourth quarter, we expect to embrace more projects.

A - Renata Battiferro {BIO 19330325 <GO>}

Next question from [Mr. Floridan Ernato]. With the exemption on the urban building and land tax that was announced by the government, how will that have an impact in your future results?

A - Helium Rotenberg

Well, this is still an uncertain area. The government had decreased the IPI, but then the [in tax] on industrialized products. So we see a balance of strength. It won't change anything in-house because the tax on industrialized products is already 0, and they also win in some other parts of Brazil. Right now, I'd say it's neutral.

A - Renata Battiferro {BIO 19330325 <GO>}

Next question from [Paulo Vasconcelos]. Considering your capital structure and capital allocation, what is the leverage level that you find to be healthy? And what are you going to do regarding the managing or generating exceeding cash?

A - Helium Rotenberg

Well, I believe that your question has 2 parts. First, regarding leverage, it's within 1x to 2x. What we find healthy for companies such as ours is exactly this 1x or 1.5x or 2x. Obviously, it's not only whether having low leverage. But as I mentioned during the presentation, we should generate more cash in the second half of the year.

That is what regularly happens. And we know that the fourth quarter is affected by December in which we see a decrease, but we will generate more cash. So our leverage level should be lower at the end of the year. But what is healthy for our company ranges between 1x to 2x because we don't want to be below that nor above that.

A - Renata Battiferro {BIO 19330325 <GO>}

Next question, [Tiago Avolf]. Can you please talk about the potential Infinix share? Do you expect a very quick ramp-up in volume?

A - Helium Rotenberg

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I really wish I were able to project the future. Whenever you launch a product, you don't know. But we believe in that product. The product line is very good. I am now trying the 5G product, and I can tell you that it's really great.

I believe that we are going to increase share. With regard to the ramp up, it will start slow, but we will increase and we will achieve our full expectations at the end of the third year. So it's a measure of a brand penetration, market penetration. We are now focusing on retail, vivo and direct sales as a first experience. So we still need to navigate that first.

A - Renata Battiferro {BIO 19330325 <GO>}

Next question from [Victor Rodriguez]. What are the potential impact on Positivo with the lockdowns in China?

A - Helium Rotenberg

Chinese components come from Shenzhen. So we faced challenges in January when that area underwent lock down for 2 weeks. We don't have many components coming from Shanghai. So we may have more difficulties if the lockdowns affect Shenzhen. But right now, that's not what we see.

A - Renata Battiferro {BIO 19330325 <GO>}

Next question by Tiago Avolf. Do we intend to accelerate the execution of our share repurchase?

A - Helium Rotenberg

Yes. We have announced a program, and we really plan on carrying it out. But now we need to comply with the Brazilian Securities Commission, that require us to be now in the silent period. But we do see this possibility, great possibility in that.

A - Renata Battiferro {BIO 19330325 <GO>}

(Operator Instructions) I don't think we have any other questions.

If there are no further questions, we close this video conference.

I'd like to turn it over to Helium for his final remarks.

A - Helium Rotenberg

Thank you very much for joining us today. Thank you for your questions. We are very optimistic. I am particularly happy with the strategy that we implemented. And I think that we really got it right, and now we are bearing it fruits.

Thank you very, very much. Thank you, everyone.

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