# Y 2014 Earnings Call

## Company Participants

- Adolpho Souza Neto, CFO
- Carlos Marinelli, CEO

## Presentation

### Operator

Good afternoon, everyone. Welcome to Grupo Fleury 2014 Fourth Quarter Conference Call. Mr. Carlos Marinelli, CEO and Mr. Adolpho Souza Neto, CFO will present the results. This event is being recorded and all participants will be in a listen-only mode during the company's presentation. After Grupo Fleury's remarks, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions)

This event is also being broadcast live via webcast and may be accessed at through Investor Relations website at www.fleury.com.br/ir, where the presentation is also available. Those following the presentation by the webcast may post their questions in advance on our website. They will be answered during the Q&A session as long as we have enough time.

Before proceeding let me mention that forward-looking statements are based on the beliefs and assumptions of Grupo Fleury management and an information currently available to the company, they involve risks and uncertainties because they relate to future events and therefore depend on circumstances that may or may not occur. Investors and analysts should understand that conditions related to macroeconomic industry and other factors could also cause results to differ materially from those expressed in such forward-looking statements.

Now I'll turn the conference over to Mr. Carlos Marinelli, CEO of Grupo Fleury. Mr. Carlos, you may begin.

### Carlos Marinelli

Thank you. I want to welcome and thank everyone for your time and attention this earnings release presentation of the fourth quarter of 2014. For us the management, the fourth quarter of 2014 highlights an evolution our objection designed for short and medium term.

First, the actions aimed at profitability, including increased strictness in controlling costs and expenses keep showing its effects as shown in the EBITDA improvement of 474 basis points higher than the fourth quarter of 2013. Even considering the non-recurring effects reported in the fourth quarter 2013, which were related to the restructuring implemented in that period. This improvement in EBITDA remains of approximately 200 basis points. In the full year, we have reached an EBITDA margin of 18.4%, 159 basis points higher than the 2013. Second, growth resumes its acceleration, especially with the continued two digit growth of Fleury brand and diagnostic operations in hospitals

Despite the fact that our lab a+ [ph] operations in Rio de Janeiro were affected by the restructuring of services offering and PSCs network and that in Sao Paulo, (inaudible) has reduced its growth during relocation to the high- intermediate segment. The company have achieved a growth of 6.5% in gross revenues and 8.4% in net revenues, consolidating its potential for qualified growth in 2015 and coming years.

Third, the management of the order to cash process together with the improved profitability enabled the company to work record operating cash flow of BRL286 million. So, the company can follow up with a conservative net debt, even handing out record dividends of BRL200 million and investing in the expansion of services offer and structuring of development of IT systems.

Fourth and not least, the company is improving its structure, its management and its processes and it is expanding its offering in the premium brands to grow even more profitable in the coming periods. After the expansion 4,700 square meters in Fleury brand making the first quarter of 2014. We are preparing new expansions for 2015 and 2016.

In addition, investments in information technology systems should enable improvements in productivity and management and preserve us as the leader in our industry in customer satisfaction, service excellence and innovation in diagnostics. Here it is important to mention that succession levels achieved higher levels in 2014, when compared to 2013. Thus despite the negative effects of World Cup in the second quarter and electoral and economic uncertainty in Brazil, we took the actions necessary to prepare the foundations of profitable organic growth in 2015 and subsequent years.

We will continue capturing the latent demand for diagnostic services of superior quality in the premium segment and bring greater profitability and competitive advantage in the intermediate segment. For the magical community including partners in hospitals, we will continue to show excellence, innovation and unique ability to diagnose resolution. And the actions to improve the administrative and operational management as the example seated in the slide three, will follow strength.

Before passing to Adolpho that will detail more the numbers, I would highlight a few points. Management of costs and expenses ended the year 2014 with the reduction of 0.5% in the absolute value of cost of services and about 3% in general and administrative expenses offsetting the inflation increase of the period.

On the slide five, we will show some further signs of our D&A of sustainability and business innovation. Those are present in the recognition of our deliveries in this things and in the launch of new diagnostics, such as the identification of the chikungunya virus. This year in addition to our continuity in the portfolio of the sustainability index of BM&F

Bovespa, the ISE, we open our questionnaire answers for public monitoring and continuous development of this highly regarded index.

I would also like to comment on the current concern about the effects of water and energy crisis, especially in Sao Paulo. Our teams of infrastructure operations and sustainability have been doing a great job preparing us to face the possibility of increased risk, having measures and contingencies in our core operations.

Today most of the units have water reservoirs for over three days and preestablish contracts with water tanker trucks and artesian well to our technical area. Diesel generators are already in place to act as energy contingency in case of shortage. In large bases and in technical area too.

I will pass now to Adolpho Souza Neto, our Executive Director of Finance. Adolpho?

## Adolpho Souza Neto {BIO 21636124 <GO>}

Thanks Carlos and good morning everyone. I will continue the presentation by showing more detail, the growth of our business lines in slides six and seven. On slide six, we show that the growth of 6.5% in gross revenue in the quarter was driven by the continuation of a two digit growth in the Fleury brand and the return to our two digit growth level in the diagnostic operations in hospitals.

In the regional brands, the growth was lower due to the repositioning of the brand a+ in Sao Paulo to the high intermediate segment with a consequent reduction of accreditation implants with lower prices.

As for Rio de Janeiro, the effects of robust service offering in labs a+ especially in late 2013 and throughout 2014, also affected that the growth of the fourth quarter of 2014. Let's remember that our focus on recovering profitability and optimization of the PSCs base match the selection of payers and a reduction of 14 PSCs in the fourth quarter of 2013 and seven additional PSCs throughout 2014 in Rio. As a consequence, and already moving to slide number seven, we see that the Fleury brand has gained share in the Group's total revenue growing to approximately 49% versus 44.5% in 2013, while revenue from Rio de Janeiro reduced its participation to less than 18%. Even though the premium brand Felippe Mattoso continues to grow.

For the year, consolidated gross revenue growth was 1.2%, with Fleury brand growing 11.4%, while other businesses had their growth affected by the profitability actions, including the effects of Rio de Janeiro's selection of payers and reduction of PSCs and in non-regional brands including Rio, we had equation of the services portfolio. It's also worth mentioning the discontinuation of the chronic diseases management business.

On slide eight, we start by the revenue per square meter, constant compared to the fourth quarter of 2013 even with the additional 4700 square meters in Fleury and 1300 square meters in a+ Sao Paulo, which are still at the beginning of their maturation.

Revenue per PSC continue to grow, resulting from the concentration of PSCs, which lead to the growth of almost 10% in the average sized of the outpatient centers. The average revenue per test continues to reflect the effects of PSC qualification mix and price negotiations close to inflation. In the last graph, we see same-store sales as a driver of growth, which will be accelerated by the maturation of the new centers of the Fleury brand in the first semester and reinforces the focus on asset efficiency and improve the product mix mentioned by Carlos.

Slide nine has the sales mix by brand of the outpatient business showing once again the business portfolio adjustment made throughout 2014. On slide 10, we detail the growth indicators by brand. For the Fleury brand, the growth of 11.4% as a component of the increasing average price per test of 4.5% resulting from mix and price effects and volume growth mainly driven by same-store sales, while the revenue per square meter decreased 1.3% due to the opening of the additional 4700 square meters in the first half of 2014.

In the regional brands excluding Rio, the repositioning of a+ brand in San Paulo had consequent reductions of accreditation affecting the level of growth mainly on imaging services, which also affects the average price per exam. In addition, the opening of the a+ unit in Braz Leme in the fourth quarter of 2014 reduces revenue per square meter temporarily. After these adjustments growth will return to higher levels with profitability already starting to respond positively.

As for Rio de Janeiro, reduction of PSCs with the closure of BRL0.21 since October of 2013 and the reduction of unprofitable imaging services also affected growth. The average gross revenue per test was reduced due to the positive volume growth in clinical analysis. In other words, the mix effect was greater than the price increase. At the same time, it's important to mention the positive growth in same-store sales and gross revenue per outpatient center, finally improvements in asset utilization.

On the next slide where we talk about the B2B business. We see a growth of 10.4% in the diagnostic operations in hospitals compared to the same quarter last year, driven mainly by the same hospital sales of 7.7% and the additional of the hospital operation in the middle of 2014, which offsets the discontinuity of the 11 small operations than in the fourth quarter of 2013.

Going to the deductions and rebates on slide 12, we see an evolution as this expenses represent 3.8% of gross sales compared to 5.4% in the fourth quarter of 2013, mainly due to the reduction of 150 basis points in the line of deductions with special note to the operations in Rio de Janeiro for the effects of the selection of payers and process improvements begins to show more significant results.

Now we will detail the costs and expenses starting with the drivers in slide 13. The first graph on the left highlights that the cost controls made in the last four quarters, resulted in a decrease of 0.5% in the annual amount versus last year and show an effective control of the cost base, especially considering the growth levels prior to 2014.

Although the number of square meters has increased year-over-year, mainly due to the expansions in the Fleury brand in the first half, the company was able to mitigate the effect and the inflation in the year with cost reduction initiatives in all areas. The process of closing unprofitable outpatient centers has stabilized and we are improving the results of existing assets in Rio de Janeiro and in the other regional brands.

The next slide shows with a little more detail, our cost of services with reductions mainly general expenses, while we continue to qualify our services working closely with our staff and our physicians.

It's worth noting, as clarified in slide number 15, that the majority of the improvement compared to the fourth quarter of 2013 is recurrent that is just a real improvement in the management of fixed cost base of the company.

Let's remember as reinforced in the third quarter conference call, that the fourth quarter is seasonally weak and we expect the next quarters to improve the dilution of this fixed costs raising the gross margin of the company, especially in the second and third quarters of 2015.

Operating expenses especially SG&A is for commodity analysis using a slide 16 as a support. Compared to the fourth quarter of 2013, we see a small increase due to the non-recurring expenses of BRL1.4 million and BRL1 million higher expenses in marketing, in line with the natural seasonality of the business.

Although not available in the slide, it's worth commenting that the increase in SG&A versus the third quarter of 2014 was the result not only of the aforementioned no recurring lay off expenses and higher spending on marketing, but also by a no recurring increase of spending on consultancies due to the payment of some remaining variable installments and the closure of an agreement with MIT, plus the differential of BRL1.5 million in the profit share -- sharing provision. In the provisions for contingencies, the comparison of the previous year lead to a disadvantage as there was in the fourth quarter of 2013, a higher net reversal of provisions.

Turning to the below the line, which starts on slide 17, this chart showing the profile of our debt, which composed mostly by the debentures issuances of 2011 and 2013 with maturities extending to 2020 and that represented BRL925 million out of the BRL1.57 billion in gross debt at the end of the year.

The cash balance at the end of 2014, was BRL505 million and therefore the Group ended the year with a net debt of BRL552 million representing a ratio of 1.8 times EBITDA close to the 1.7 ratio observed in the previous quarter and at the end of 2013. The financial results for the year was a net expense of BRL36 million compared with BRL42 million in 2013. Reduction that happened despite the increased interest rates and the decrease in the cash available for financial investments mainly due to the non-recurring credit of 10.7 million recognized in the first quarter of 2014 related to the reversal of the ICMS provision on imports of machinery and equipment. Without this credit, our results would be net financial expense of BRL47 million in the year.

On the next slide number 18, we see the breakdown of our rate of income tax and social contribution, which in 2014 was 40%, all of it on the deferred tax, since the use of the tax credit of the goodwill on acquisitions led against our cash tax equal to zero.

Which can also see in the next slide number 19, where we see that the net income in the quarter was BRL12 million, thus reversing the loss in the same period of last year and leading to an annual net income of BRL86 million, an increase of 40% compared to the year 2013 or BRL144 million excluding the deferred tax the so-called net cash income representing therefore a 8.6% margin in relation to net sales in the year, compared with 6.7% in 2013.

The Group's EBITDA ended the year at BRL308 million and a 11% growth compared to 2013 and a margin of 18.4% of net sales, an improvement of 159 basis points compared to 2013.

The next slide, number 20 shows the profile of our accounts receivable at the end of the quarter, where we show reduction of our gross accounts receivable balance of BRL46 million against the same period last year.

Despite the increase in gross revenue of 6.5% in the quarter and as a result of the conclusion of the negotiations with operators and the write-off of receivables that we already provisioned and improvement in our aging profile with the reduced participation of the range of outstanding debt for more than 120 days down to 18% of the gross accounts receivable the lowest percentage in the last 10 quarters.

Moving on to slide 21 cash flow. We see that our operating cash flow in the quarter was BRL87 million and in the year BRL286 million, a record amount in the company's history. And that represents the conversion rate of operating cash to EBITDA of 93% in 2014, mainly due to the increase in cash earnings and improvements in working capital management. Both in receivables as previously mentioned as the suppliers and inventories.

Investments in CapEx, which are detailed on the next slide, totaled BRL118 million in the year focused on our expansion program of Patient Service Centers and services that accounted for 45% of the total spending and spending on IT projects, which represented 35% of the total.

We also present our capital budgets for 2015 of BRL189 million, which we continue to focus on investments in the expansion of PSCs and services mainly in the Fleury brand. An investments in strategic and restructuring projects, which will enable the company to continue the improvement of its operational efficiency and sustainability of its operations.

We will now turn to the question-and-answer session.

## Questions And Answers

## Operator

Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions) This concludes today's question-and-answer session. I would like to invite Mr. Carlos Marinelli to proceed with his closing statements. Please go ahead, sir.

## A - Carlos Marinelli

Again, I want to thank everyone for the time and attention in this earnings release and say that while we have a challenging year ahead our confidence is great. As the company's management we are in the right path, because we're making choices that enhance the future prospects that lie ahead.

A lot of work, reorganization and dedication of all of our teams built the results of 2014. Part of this improvements can be read, seen and felt. We will continue committed in our purpose of bearing higher profitability margins not only through the better management of costs and expenses, but also through the best positioning of our services and relationships with payers.

It's our firm commitment to bring sustainable growth for the company through the continuity and renew of our values of excellence, quality and innovation. I will remain available through our Investor Relations team and will be a pleasure to meet you in future opportunities. Good afternoon, everyone.

## Operator

That does conclude the Grupo Fleury audio conference for today. Thank you very much for your participation. Have a good afternoon and thank you for using chorus call.