Q3 2015 Earnings Call

Company Participants

- Jose Carlos Wollenweber Filho, Chief Financial Officer
- Luis Fernando Memoria Porto, Chief Executive Office

Other Participants

- Mario Bernardes Junior, Analyst
- Unidentified Participant

Presentation

Operator

Good morning. Welcome to this conference call in which Locamerica will present its results for the third quarter of 2015. We would like to inform you that during the company's presentation, callers will only be able to listen. Later, we will move into the Q&A session when further instructions will be given.

This quarter Locamerica will also have some time to take questions from the press right after the Q&A with market analysts. (Operator Instructions) This conference is being simultaneously translated into English and questions maybe asked normally by any participants who are connected from abroad.

Questions may also be asked online through our webcast platform. We remind you that this conference call is being recorded and will be made available on the company's website and up to 24 hours. If you do not have a copy of Locamerica's release, it maybe obtained on the company's website at locamerica.com/ri. This conference call and the slide presentation are also being broadcast online and can accessed on our company's website.

Before we continue we would like to clarify that any statements during this conference call about the company's future business perspectives, as well as projections, operational and financial goals and its potential growth are merely predictions based on the management's expectation on Locamerica's future.

These expectations depend on our industry's performance, for those overall economic performance, and domestic and foreign market conditions. They are therefore subject to changes. We have with us today, Mr. Luis Fernando Porto, CEO; and Mr. Carlos Wollenweber, CFO and Investor Relations Officer.

I would now like to give the floor to Mr. Luis Fernando Porto. Please, Mr. Porto, you may proceed.

Luis Fernando Memoria Porto {BIO 17590082 <GO>}

Good morning, everyone. It's a great satisfaction to present today Locamerica's operational and financial results for the third quarter of 2015.

Before going to our results, I'd like to briefly highlight some industry trends observed during this quarter. Slide three shows the credit scenario is still restrictive for vehicle financing plans. Despite seeing a drop of 0.4% in the segment defaults rate which went from 4.4% in Q3 2014 to 4% in Q3 2015, the graph to the right shows that funds available for vehicle financing plans decreased by 18.4% in the third quarter of 2015 year-on-year.

Lower credit availability as we can see on slide four, created a direct impact on new cars sales. The upper left graph shows that new light vehicle sales dropped 21.7% in the first nine months of the year when compared to the same period in 2014. The same graph shows that used vehicle sales have remained robust and even have gone up by 2.4%.

We believe that besides the lower dis-availability of credit, we mentioned before, part of this diversion behavior between new and used cars can be explained by an increase of new car prices which according to the IBGE was 5.8% from January to September this year. This was also due to the reinstatement of the IPI and the inflation and exchange rate.

The increase in spread between new and used car has motivated a migration in demands favoring used cars. At the lower left hand graph shows the last month's sell ratio for used cars in regards to new cars went up to 4.4 times, our highest recorded level. The right-hand graph shows that the nine-month of 2015 have shown that Locamerica had a performance so higher than the used markets as a whole, hence our sales figure grew 18% year-on-year.

Despite that, our market share accounts for only 0.13% that means that if there is a slowdown in the demand for used cars, would be able to offset the amount of sales by increasing our market share. Moving onto our operational highlights, slide six shows the overall value of new rental contracts signed in Q3 2015 which is R$92 million, 2,083 cars.

The commercial pipeline for the next three months has been steady with approximately 23.2 thousand cars in tender up 6.5% since the second quarter of 2015. It's worth reminding that despite having this pipeline, due to uncertainties in Brazilian economy, we've noticed companies are slower to sign contracts, which in turn delays this pipeline from materializing into actual contracts.

Slide 7 offers a breakdown of our fleet, which closed the quarter with 29,325 cars, a reduction of 3.2% year-on-year. The operational fleet has decreased by 8.6% in this period, coming to a total of 22,730 vehicles by the end of September. As we'll see soon, we were able to partially offset this reduction maybe operational fleets [ph] this quarter with efficiency gains and a better utilization rate.

It's also important to highlight that at the close of quarter, three, the fleet was already higher than the one we had in quarter two, and it's also worth highlighting, its helped your makeup which already presents proportionally more vehicles in operations and deployment with a lower car inventory.

A high number of cars in deployment in the case are growth of the operational fleet in the near future, as soon as customization has concluded and cars are made available for clients. The right-hand graph shows that at the end of this quarter, fleets decommissioning will normalize in absolute terms with a reduction of 454 vehicles on storage, as well as its total fleet yield EoP which at the end of September reached 10.8%, a reduction of 3.4% from the spike during Q1, 2015.

As you'll see in the following slides in Q3 2015 we were able to reduce our inventory without reducing sales prices. Since we have record margins for used cars this quarter. We can see it on slide eight that the company has sold 3,074 cars in the third quarter 2015, up 9% Q-on-Q while the number of decommissioned cars had a reduction of 40% in comparison to the fourth quarter of 2014 going back to the levels we had in last year.

I'd now like to give the floor to Mr. Wollenweber, CFO who will give us our financial highlights.

Jose Carlos Wollenweber Filho {BIO 16884477 <GO>}

Good morning. It's a great satisfaction to show you our financial highlights for this quarter. Slide 10 shows our net rental revenues, which were a total of R$97 million this quarter, and 291 million in the nine months 2015, a growth of 7% year on year which was a reflection of an increase of 9.6% in our average monthly rate, a slight reduction of 1.9% in the amount of daily rates.

This increased rate reflects, the readjustment for ongoing contracts and an increase in new car prices and interest rates for new contracts.

The next slide shows the number of cars sold by Locamerica totaled 3,074 units this quarter up 9% quarter-on-quarter. The average price went up almost 18% year-on-year to R$26,500 this is the result of a change in profile to higher value added vehicles, as well as higher share of sales from the retail channel, which now represents 35% of our total sales in comparison to the 26% we had in the second quarter.

As a result, this quarter we delivered a net revenue of 81 million Brazilian cars for used -- sorry, R$80 million for used cars totaling R$238 million so far this year, a growth of 28% and 33% respectively. Slide 12 shows the comparison of our margins in Q3 2015, our car costs and maintenance have decreased by 3.1%, a reflection of more efficient cost management and a reduction in the average age of the fleet.

Our SG&A expenses increased by 2.2% and it's an important to highlight that we have intensified our credit analysis area and since the beginning of 2015, we have become more rigorous in our internal charging processes.

In the used car segment, we had the biggest gross profit since the company's IPO, R$5.7 million in the third quarter and 3.8 million in the accrued value this year. As a result, we have delivered an EBITDA with a margin of practically 58%, 5.6% above what we reported in the same period in 2014.

This increase was offset by depreciation expenses, a consequence of the increase of higher value added vehicle participation in our fleet, meaning we had an improvement of 3.4 in the EBIT margin which reached 32.8%. Slide 13 shows that the average age of our fleet is 15.9 months, which was 1.1 month below what we had in Q3 2014. Also this quarter we had an utilization rate of 96.4%, the highest since the first half of 2012.

The next slide shows the financial results. Financial expenses increased 14% this quarter in comparison to the same period last year. This is due to the increase in interest rates and a more conservative liquidity strategy. Considering the current macroeconomic scenario, we've decided to advance the issuance we have for next year meaning that this quarter our cash flow in costs were considerably increased.

Slide 15 shows our capital structure. Our financial result is now approximately R$30 million and our leverage has dropped 3.17 times net debt for EBITDA. We closed the quarter with R$325 million in cash which was higher than what we had in 2015 and 2016.

We're highlighting that we continue to have very competitive debt -- average debt cost of CDI plus 1.5% of vehicles offered as collateral at 16%.

Questions And Answers

Operator

We are now moving on to our Q&A session. (Operator Instructions) Our first question is from Mr. Mario Bernardes Junior from Banco do Brasil.

Q - Mario Bernardes Junior {BIO 17363553 <GO>}

Good morning, Mr. Porto, Mr. Wollenweber. I have two questions; the first is about the used car margins, I think that your management policies was good -- just mentioned due to the retail channel and I just like to know what this level will be like in the future. Thank you.

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

Good morning, Mario. Thank you for your question. While we had already been working on new cars for some time and we were focusing on two main actions, increasing the depreciation rates, and also investing strongly in a new channel which is a retail channel.

These two actions are now starting to bring better margins in sales for used cars. Since it's the first quarter, we can't really state that this would be our new established level that will be stable for the future, but what we can say is that from now on we will have positive results in the used cars line.

Our EBITDA will be positive and our margins will be positive. It's still early to talk about our level in terms of percentages and so on, but you can rest assure that we will report better margins in sales for used cars. I think that's something that we feel very comfortable in saying.

Q - Mario Bernardes Junior {BIO 17363553 <GO>}

Thank you. My next question is -- well, can you tell us a bit more about the competitive environment, how are bids going, what about prices, just tell us a bit about the current scenario. Thanks.

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

Thank you. Well, the scenario, we've been going through a hard moment in the economy as a whole, this is not different in our industry. Banks and credit channels that are available in the market are becoming much more restrictive which means that it's more difficult to get financing plans approved.

This is not the scenario for Locamerica, we just had an issuance, we have a reinforced cash structure, our debt payments and our investments in cars and an expansion are going to go until the end of 2016 and that's why we're going through such a great moment. Of course, that's not what we have seen in most of the market especially mid-sized and small competitors, they have really been taking the blunt of this recession.

We've been having hard time paying their debts or making the necessary investments. So, the competitive environment, on one side shows a reduction of the businesses we got due to the macroeconomic conditions, but on the other side, we also have less competitors right now, so of course, big competitors are not going through this problem, which means we and four others are not having problems with investments, but most of the market is growing through funding problems.

So competitive environment is basically the same as we saw in the last three quarters, it hasn't improved, but it hasn't worsened either.

Q - Mario Bernardes Junior {BIO 17363553 <GO>}

Do you think that these smaller competitors might be taken out of the market?

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

Definitely, yes, of course I'm not going into main names, but some smaller and mid-sized companies are already practically out of the market, we have some monitoring programs, pipelines and we see a reduction in the number of competitors we have in the market which clearly shows that some companies of course smaller ones are unable to cope with the market.

Q - Mario Bernardes Junior {BIO 17363553 <GO>}

And of course this is going to translate into greater shares for you, right?

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

No, we don't necessarily expect to have growth because of tax right now. We're being cautious due to cash location and credit analysis, we're becoming more restrictive in that right now, we can't allocate capital, but deciding where and to whom is still a difficult position. The scenario is stable. We're not sure if that's going to give us a greater market share, but we think that unfortunately that helps in one sense, but in other sense it makes things more restrictive due to mixed macroeconomic conditions.

Q - Mario Bernardes Junior {BIO 17363553 <GO>}

Okay, thank you.

Operator

The next question was sent by Enrique Fleming (inaudible). In terms of capital allocation, wouldn't it be better to repurchase shares instead of paying dividends, since the company has been traded at low levels?

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

Well, both things are not directly connected, Enrique, obviously but I'd like to thank you for your question, but these things are not directly connected. We had a repurchasing program last year and obviously shares are under the value we see as reasonable. So this program had as it's aimed.

Q - Unidentified Participant

Do you have a percentage of the company in house? So that when the stock option programs we have with other executives when we wouldn't have to dilute the company's shareholders?

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

So its function was very specific and we were able to meet the goals of that program. Now JCP is distributed due to fiscal benefits and not necessarily any other reason.

The company right now is 100% focused in giving priority to its cash position. We think that we're going through a very difficult complicated moment in the economy in Brazil and our main efforts right now are directed to preserving our cash position and that's the main reason why that happens. JCP give us fiscal benefits which are important, so we decided to keep the same powers in. Thank you for your question.

Operator

The next question was also sent via webcast by Rodrigo Glatt, [ph] GTI. What impact do you see in the liquidation of the CS loans in the beginning of 2016? Do you think we will be able to get contracts from smaller competitors who are facing hardships? Thank you.

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

Good morning, Rodrigo. Thank you for your questions. First of all that debt represents 16% of our debt and its liquidation should happen now in April, and I don't think it will create a bigger impact to our debt spread impact [ph]. The second question, Locamerica today is doubtlessly trying to spread contracts, so we are focusing on smaller and mid-size clients which are usually certified smaller competitors. So that goes hand in hand with our commercial policies and it's also, it's favorable due to the moment that these smaller companies are going through. However, as I said in the previous answer, we're much more selective now, and of course credit limitations are also a limiting factor for us.

But we're trying to find the best opportunities and we're trying to select the best clients right now to allocate our capital in a better way and of course and to increase our profitability.

Operator

(Operator Instructions) If there are no further questions, this concludes our Q&A session with market analysts. We would now like to give the floor to Mr. Porto for his closing remarks before the press Q&A.

A - Luis Fernando Memoria Porto {BIO 17590082 <GO>}

Well, I'd like to thank you all for listening in and I like to highlight that the company will continue to work to minimize the impacts of our difficult economic situation. We're going to continue to be based on a resilient rental business with a very objective value proposition, which is also a great opportunity for our clients to cut and reduce cost. The next quarters will continue to be challenging, but we believe that throughout 2015, we took all measures necessary to ensure greater operational efficiency and a differentiated capital structure. We would like to have you again listening to us for the next results call, and once again, our Investor Relations team is at your disposal for any questions you may have. Thank you and have a nice day.

Operator

If there are no further questions, this concludes Locamerica's Conference Call. Thank you for participating and have a nice day.