

Y 2018 Earnings Call

Company Participants

- Clovis Poggetti, Chief Financial Officer
- Gabriel Mariotto, Head of Business Analytics
- Paulo Rogerio Caffarelli, Chief Executive Officer
- Victor Schabbel, Head of Investor Relations

Other Participants

- Alex Spada, Analyst
- Carlos Macedo, Analyst
- Craig Maurer
- Felipe Salomao, Analyst
- Jeff Cantwell, Analyst
- Mario Pierry
- Neha Agarwala, Analyst

Presentation

Operator

Good afternoon everyone and thank you for waiting. Welcome to Cielo Fourth Quarter of 2018 Results Conference Call. With us here today, we have senores Paulo Caffarelli, Clovis Poggetti, Victor Schabbel and Gabriel Mariotto. This event is being recorded and all participants will be in a listen-only mode during the company's presentation.

After Cielo'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 through Cielo website at <http://ri.cielo.com.br/en/>, where the presentation is also available. Participants may view the slides at any order they wish. The replay will be available shortly after the event is concluded. Those following the presentation, via the webcast may post their questions on our webcast. They will be answered by the IR team after the conference is finished.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of Cielo management and on 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 macro-economic conditions, industry and other factors could also cause results to differ materially from those expressed in such forward-looking statements.

Now I would like to turn the conference over to Mr. Paulo Caffarelli, Mr. Paulo, you may begin your presentation.

Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Okay, thank you. Good morning all and welcome. This is my first time at Cielo's earnings conference call. And I'd like to thank you, our shareholders, our employees, and also our VPs, Vice Presidents that support our business on a daily basis.

Joining me today to discuss our results are Clovis Poggetti, our CFO; Victor Schabbel, our Investor Relations Director; and Gabriel Mariotto, our Business Analytics Director. I want to start by reinforcing that Cielo is the sole leader of the payment industry in Brazil. And for sure, it's the company that is best, equipped to continually holding this leadership.

When, we look at the numbers, we have published to-date. We will be able to see that from our Q1 -- for our Q4, on, we are back. We are back to the game, and we are back stronger. This comeback requires adaptation and resilience. It requires us to make a choice between margin and market share. At this moment, maybe the moment with the strongest competition in the industry, we are strategically choosing market share.

The industry battle will be won -- by those who can adapt accordingly to these new moments and these moments require that players deliver additional attributes to an increasing commoditizing product. From our side, we've already begun our adaptation, and there is still more to come. I want to share some of the actions we have already made. Revamping of our pricing strategy. We need to be more competitive, we need to be more competitive to be back to the game. hiring of 1,000 new sales executives, targeting the acquisition of 2,000 new customers a day, and even more will come.

Hiring of 500 to act exclusively, with micro entrepreneurs segment. Cielo will compete in every segment, as few can do. Indeed, this is very important for us because when you analyze our competitors in Brazil, perhaps Cielo is the only company that currently are actuating in the -- in all the segments. We have broke the paradigm of selling terminals at Cielo. Cielo is already selling its terminals portfolio and also has an additional brand, Stelo as our fighter brand. As I said before, our industry product is highly commoditized and adding value to customers is the strategy to win the game.

In that sense, and in our point of view, there are key initiatives we are focusing this year. High availability by IT, convenience in commodity, a trusted brand that is the top of mind in the industry for years. Since 2014, Cielo has been the top of mind in Brazil in terms of payments company. Reinforced marketing investments and above all, improved even more our service.

Improving our service implies, an effective and fluid [ph] the customer journey, we the 3,000 Cielo employees, named in 2019, as the Year of the Customer Relationship. This is a commitment from all of us, with the increasing improvement in our services and this is impacting even our variable pay. We decided that we increase the volume that we need

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to consider when we will define the pay for employees, relating to the customer experience.

On the top of that, we've hired a specialized consultancy firm to help us rework the company. We are focused and always working for operational efficiency. Our structure has to properly reflect our ability to generate results, without jeopardising, the quality of our service. And also very important, we are identifying our digital evolution capabilities, considering how fast it's transforming our industry. And we are also, intensifying the constant and required improvements for our products and services.

So finally, I'd like to reinforce that we are back into the game. We will defend and strengthen our leadership by delivering against our shareholders' expectations. Having a work climate, and above all, granting our customer satisfaction. As a final remark, I'd like to ratify our commitment with the future value generation in medium and long-term. This is very important for us because, as you could see, our guidance for this year going to be between BRL2.3 billion to BRL2.6 billion. It's different than the other results in the past. But for us, it's very important to focus nowadays. In March -- or excuse me, in market share instead of March because market-share is going to put the Cielo, as a competitive company among the other -- the other peers in Brazil. In this case, we need to be competitive, we need to be prices -- adequate prices for -- to be involved in this competition.

I'll pass to Gabriel Mariotto, now that will talk about the retail for us. Thank you.

Gabriel Mariotto

Thank you, Caffarelli. Good morning everyone. I'm happy to share with you the most recent numbers about the retail sector in Brazil. As indicated by our Cielo Broad Retail Index, the ICVA, results for the Brazilian retail sector in the last quarter of 2018, were very positive. The inflation discounted in index accelerated to 3.6% from 2.2% in the third quarter, on a year-over-year basis. In nominal terms, the index also advanced from 5.7% to 7.5% in the third and fourth quarter respectively. Black Friday was a positive highlight, resulting in a year-over-year growth rate, higher than the run rate posted by the retail sales before the event.

The Christmas season in general, also outperformed, though not to the same extent as Black Friday. Thus 2018 ended with a deflated consolidated growth rate of 2.5%. The first annual real retail expansion, since 2014, ending a three year series of real decreases in the index. This result confirms Brazil's retail sales upturn.

One we had previously noted over recent quarters, despite the one-off events, which negatively impacted retail sales in 2018, especially in the first half, such as the trucker strike and the World Cup. Retail continued its overall come back and then ended the year, with a performance very close to the levels last seen in 2014.

Another positive was the fact that this resurgence was geographically broad based, enjoyed throughout Brazil. All five macro-regions, accelerated their pace of growth, on a

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year-over-year basis and all of them recorded real growth compared to 2017. Even the region of greatest relevance, the Southeast which -- with its highly diversified economy and does a higher inertia to recovery, went from a shrinkage of 0.7% in 2017 to an expansion of 0.9% in 2018, on an inflation discounted year-over-year basis.

Only the Midwest and Northeast regions showed signs of a more tepid comeback though -- these regions also advanced in 2018, consolidated returns in the last quarter of 2018, they slowed pace quarter-over-quarter. Results across it specific retail sectors were more uneven. On the one hand, the supermarkets and Epermarket sectors, which is the index most representative one, recorded an impressive acceleration continuing their upward trend initiated in mid-2017, especially after a substantial decline in food inflation.

On the other hand, the food service [ph] sector, for example sustained the same level of growth seen in 2017, which is in-fact shrinkage. The fuel stations, sector saw double-digit growth, nominal growth in the second and third quarters. But largely driven by a strong price increase. Real 2018 growth for this sector still came in negative. When we analyzed the relevant sectors, more related to the sales of durable and semi-durable goods such as furniture, home appliances, department stores and building materials all saw growth recovery.

Though the apparel sector's rebound was milder than the rest. Therefore, although -- we cannot give any estimate for 2019, the overall recent retail sales trend is generally positive, for all the retail segments across the Brazilian economy. Lastly, a quick reminder that the ICVA represents retail sales performance as a whole, not specifically the current market nor Cielo's results.

Thank you all for your attention. I'll now turn it back over to our CFO, Clovis.

Clovis Poggetti {BIO 16529642 <GO>}

Thank you, Gabriel. On the next slide, I will discuss a few of our operational highlights. In the fourth quarter of 2018, when we consider volumes excluding the Agro product, and the effect of volumes captured under the Multivan model. We had a slight growth of 0.1% year-over-year. This reflects the loss of a few clients in the large account segment, while, we saw a gradual recovery of our volumes in the SME segment.

On the graph to the right, you can see the performance of our POS base. To simplify the discussion, and align our earnings release, with the strategy that we are adopting, we can see here our installed POS base split and to turn out that we are either rented or sold. Depending on the segment that we are providing services to, the best solution is to offer the rental or the POS sale.

In order for us to be the most effective, especially in the entry segment, we will adopt both of our brands, Cielo and Stelo to offer POS sales solutions. For this reason, in the rented POS base, we can see a small positive growth, which is in-line with our expectations. Here I wanted to point out to you all that, this is the first sequential growth of the rented base after three years.

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This growth, although modest, gives us the comfort to say that we are in the right direction. I remind everyone that this is the first sign of our strategy since, first, we delivered the POS, the next step of the volumes that are kept by our POSs, and then we add other value-added products and services. This is the day that is mostly exposed to the SME segment. In other words, the middle of the pyramid.

In the micro entrepreneurs segment, we have the POS sale, as the most appropriate solution. Here results were significant with substantial sequential growth. Cielo's total installed base of POS reached 1.8 million terminals, speeding up the sequential growth, which reached almost 10% quarter-over-quarter.

On the next slide, you can see details on the performance of our POS sales operation. Today, mostly made by Stelo, Cielo's firebrand. In the fourth quarter of '18, we recorded sales of 286,000 POSs, a sequential growth of 175%. When we look at captured volumes, we recorded BRL1.3 billion in the fourth quarter alone, with the total accumulated in the year reaching nearly BRL2 billion.

If we analyze fourth quarter results, we would have acquired and capturing approximately BRL5 billion, which is a very relevant industry figure. Due to the pace of expansion, we have been able to sustain, we should rapidly increase our presence in the long-tail segment. On the next slide, number five, I will highlight Cielo's financial results in the fourth quarter. Net revenue was down 0.8% year-over-year, mainly impacted by the contraction of our acquiring business, as well as the Cap on the interchange fee for debit, that was imposed by Central Bank as of October 1st, last year, which impacted Cateno's results.

On the graph in the middle, you can see already the outperformance. Our acquiring businesses is still facing a challenging competitive environment, which made our EBITDA decline 20.8%. The same for margin, which stood at 36% in the fourth quarter versus 45% at the same period of the previous year. The deterioration seen in our figures, comes from these competitive environment, where we have been, assuming a more proactive attitude and with more aggressive price.

At this moment, we have been working to resume growth in reinforce our position in the Brazilian market. Therefore, besides more competitive prices, we have been investing in new marketing and hiring other sales executives to gain greater efficiency in the SME segment, again those in the middle of the pyramid. On the graph to the right, you can see that our net income came to BRL724 million in the fourth quarter, down 30% year-over-year.

Here, key drivers were the reduction in rental revenue and the commissions at Cielo Brazil, the lower results in the prepayment of receivables and the impact of the cap on the interchange fee at Cateno. After this brief comment on our results, now, I'll hand the call to Victor.

Victor Schabbel {BIO 17149929 <GO>}

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Thank you, Clovis.

Following the approach, that we took in previous quarters, we are going to talk a little bit about the revenue, yield evolution in the following slide. For the sake of time, I would concentrate here, my attention on the chart on the right side of the slide, where we have our revenue yield evolving from 1.01% in the previous quarter to 0.96% during the fourth quarter, 2018.

One of the main factors, that played against our revenue yield was once again the rental of POS terminals. Here we had a pressure again on prices mainly due to the discounts that we have been giving in the SME segment in order to be more effective. As a positive, we had a few factors. The smaller ones were; first, the mix of product with credit outpacing debit during the quarter, adding 1 basis point as a positive contribution to the yield, followed by the quick credit payment product or Receba Rapido product that added another 1 basis point and the biggest positive factor that we had during the quarter was the effect coming from the cap on the interchange fees on debit.

Although, the revenue yield talks about or covers rental and the upper credit and debit. The debit alone, the cap on the interchange fees, added 6 basis points during the quarter, favoring our revenue yield. This however was more than fully offset by the decline in prices, result of our clear aggressive strategy that we have been implementing since late August. The idea here is to be increasingly effective in the SME market at the same time that we start exploring, also more effectively the low-end of the market, the base of the pyramid, the micro entrepreneurs.

As a result, we have this effect, we have this contraction in our revenue yield, something that we should expect to be sustained going forward.

Given that, I talked a little bit about what we should expect in the following slide, let's discuss a little bit what happened during 2018. We had a guidance that had first an expectation for volume growth in our acquiring business Cielo Brasil. According to our estimates, that we set at the beginning of the year, we were expecting a growth of 5% to 7%. However, we delivered a 3.1% volume growth during the year, mainly as a result of the more competitive environment that we faced starting in late first-half of the year and mainly throughout the second half of the year. This was one of the reasons why Cielo decided to be more effective in its pricing strategy being more aggressive and now the company is taking the position of leading this aggressiveness move going forward.

In terms of the costs and expenses, we met our guidance, the expectation was for Cielo Brasil and Cateno's, total expenditures should grow by 2% to 4% in 2018. The growth was about 3%. In terms of the investments, we had a range of BRL300 million to BRL400 million and we also met this expectation investing BRL330 million. Clearly hearing the feedback from The Streets, talking to you, investors, this type of guidance was not anymore fulfilling the needs of the market. It was not clear enough for you guys to have a view on what to expect and this was the reason why we announced a different guidance for 2019.

As Caffarelli mentioned in his initial remarks, I'm here disclosing the guidance for 2019, which is an expectation of earnings -- consolidated earnings, which compares to the reported figures that we have been disclosing between BRL2.3 billion to BRL2.6 billion for 2019. So we can provide in a very straightforward way, an expectation for the year, a year that will be once again marked by Cielo, being back to the game, being more aggressive and being more effective and allowing everyone to be on the same page in terms of earnings expectations.

So now with all that said, I leave the floor for the question-and-answers session.

Questions And Answers

Operator

Thank you. The floor is now open for questions. (Operator Instructions) The first question today comes from Felipe Salomao with Citibank. Please go ahead.

Q - Felipe Salomao {BIO 19237023 <GO>}

Hi, good morning, Caffarelli, Schabbel and Clovis. Thanks for the opportunity to ask questions. Caffarelli, I have a question specifically about Stelo in my promotions. So you said that Cielo will start to sell POS devices with the Cielo brand to SME clients very soon and that Stelo will become the combat-brand of Cielo.

So my question is what would be the relevance of Stelo and also the relevance of my promotion clients to the company as a whole. Now that Cielo decided to sell devices with the Cielo brand and also given that the company's main goal is apparently to recover the market share losses in the SME business. Specifically, you mentioned that marketing expenses are going to go up this year. So can you please quantify what should be the marketing budget to our 2019? And also how this budget should be split between the Cielo brand and the Stelo brand. Thank you very much.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Okay, thank you, Salomao. The first-of-all, we decided to have specific machine from Cielo, just because we decided to start selling machining in Cielo, because there is no conflict with the rental and sell machines okay.

In this case, we have a portfolio from Cielo, but also we had a portfolio from Stelo as well. In this case, because Stelo is doing very well in terms of -- and its performing very well among our bank's partners as Banco do Brasil, Caixa, Bradesco. In this case, we decided to maintain to remain with the portfolio from Cielo and portfolio from Stelo. In this case, it's very important for us to have the both portfolios because, Stelo is a kind of combat brand.

In this kind of combat brand, you have a less price. Okay, because this is that we define it, that we're going to maintain this. Perhaps we are establishing a mix between both for -- to run 2009 [ph] -- '19. But perhaps the first quarter, you can have more a specific situation,

considering that we are just starting with the Cielo machines. I don't know if Victor would like to add or Clovis?

A - Victor Schabbel {BIO 17149929 <GO>}

I would add here Salomao, in order to more clearly explain the strategy going forward. The idea, as Caffarelli mentioned is to explore both brands, leveraging on the fact that Cielo has a huge brand awareness that put us in a position that can make us, let's say, grow faster right now -- than if we were to wait as to build up Stelo as a brand to be widely-recognized in the market.

So this is one thing. So we are going to take advantage of the brand awareness at Cielo to sell the devices aiming at the low end, just like Stelo. Stelo will continue to keep its focus there in its segment as well. But the idea is to basically offer lower prices being the fighter brand, the discount brand. So we have to maintain this approach and we are going to leverage the position there through Cielo as well.

In terms of marketing, just for you to get a sense, we are not going to disclose precisely here, how much we are going to spend in one or in the other brand. Basically because this is strategic, but what you have to bear in mind is there will be investments in Cielo. Right for Cielo to keeping the most recognized brands in our market, right. This remains being like that. And also for Cielo to be recognized at the low-end, as well and there will be more specific investments in marketing. At Stelo, in order for this brand to leverage on digital channels, right. Taking advantage that we are spending a lot of money at Cielo. And in order for Stelo to be linked somehow to the efforts here at Cielo, we are going to spend more in digital channels there at Stelo than through conventional media.

The fact is that the marketing budget is bigger for 2019 than it was for 2018. So we should expect growth in marketing expenses this year. It should be somewhat relevant growth in marketing expenses.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Let me add one thing. As Victor said, if you would remain just with the Stelo, we will do invest a lot of money. In this case, we prefer to move this money for investment in marketing just from Cielo, just to reinforce our participation in all of the segments.

Q - Felipe Salomao {BIO 19237023 <GO>}

Perfect, Schabbel, Caffarelli, thanks for the answer. If I may just one follow-up, can you please provide us an update about the development of the complementary products that Stelo aims to offer as well, such as the digital account, the prepaid card. I mean, how these capabilities are at this point? Are they fully operational and fully comparable to the market leader in the my promotions segment? Or the product still needs to -- I mean or something still needs to be developed, so that you guys can have a similar product to the market leader.

A - Victor Schabbel {BIO 17149929 <GO>}

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Thanks again, Salomao. This is an important product for us because prepaid cards have been the most important way for us to affiliate merchants in the low-end segment. Right. So micro-entrepreneurs have been choosing the prepaid cards compared to the other alternatives. For example, receiving the money in our regular banking account. And in the last three months, we launched the digital account here at Cielo, which has already over 30,000 clients using it. So now, on top of just using the prepaid card for you to spend the money, through a POS terminal, you can make wire-transfers. So transferring the money from your prepaid card through a banking account. And also you can withdraw money through the ATMs.

So we are now at the same level of our competitors. So there is no gap on a product standpoint in this segment. So the expectation is for us to keep the pace, to keep growing fast in terms of the sale of devices with more prepaid cards, active digital accounts. So there is a big room here for us to keep up the pace and growing this segment that is quite promising.

Q - Felipe Salomao {BIO 19237023 <GO>}

Okay, thank you Schabbel. Thank you for the answers.

Operator

The next question comes from Craig Maurer with Autonomous Research. Please go ahead.

Q - Craig Maurer {BIO 4162139 <GO>}

Yeah. Good morning and thanks for taking the questions. Regarding the POS sold in the quarter, it seems that the activation rate remains quite weak at around half. And so, I'm wondering if that is a concern that perhaps you're giving away hardware and not seeing it activated and those merchants are going with another provider.

Secondly, you just mentioned, you are getting into equivalents with your competitors in micro merchants. But are you planning to also launch lending products, because that seems to be the next step and globally. That seems to be very important to that segment. And lastly, because I might as well get, get them all out first, is within the middle market, are you fully phased-in -- in terms of all the actions you're taking in terms of pricing across MDRs, rents and prepayment or is that still an ongoing process. Thanks.

A - Victor Schabbel {BIO 17149929 <GO>}

Hi, Craig. Here it's Victor, sorry. So in terms of the POSs that are being sold, as we disclosed during our presentation and Clovis mentioned this precisely. The pace has been quite strong in terms of POSs sold. We have here two factors that we have to bear in mind. We have; first, the lead time for the deliveries to happen, right. So it can take up to 10 working days for the clients to get the device and this as a result postpones, a little bit the activation process. And after the client gets the device, we have to wait the client to make the first transaction, so we have the POS classified as active. Right.

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So we have been -- as you have been following us taking very conservative methodologies for us to keep tracking our POS base, no matter if it's sold or rented. So this is the approach we are taking here as well. So the good news is that, although we are selling a lot. There is some lag for these POSs to enter our POS base. So we have already some -- let's say, growth contracted for the upcoming quarters. Given the pace of sales that we had in the fourth quarter.

Right. In terms of the activation level, we have our benchmarks. We are close to them. There might be room for some improvements, but the activation rates are close to 70% of the POSs sold. This is -- give or take metric. So this is just a reference for you to know. But this is good compared to our legacy business, this is very good compared to what we have been seeing in our -- let's say the companies that we use as a benchmark.

On top of it. Talking a little bit now about the SME segment. We will continue with our effort to position ourselves in a very competitive way, being aggressive in pricing, reacting to the approach of third parties. Right. If the other players start lowering the prices, following our approach, we will have to adjust them once again and this is what has been happening. This is what we are now doing. What we are -- let's say, answering your question. If we are fully ready to explore the potential in that segment. I would say that in terms of sales force, we are very happy with the results of the 1,000 salespeople that we hired to be hunters in the SME segment alone. They are with us, since the beginning of January and the first results are promising. If we need we would hire more people in order to explore it. But so far, the results are positive.

The only thing that we are still waiting for doing and we are not going to provide any precise schedule here because it's strategic, is about the investments in big marketing campaigns, mass media being used to attract more clients. But soon, you probably will be seeing that. So I would see, this as the last mile for us to be full power in the SME segment throughout 2019 in order to regain the growth recover, the client base and start growing the volumes once again.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Craig, this is Caffarelli, I may add one thing here, related to the Cielo selling POS, it will be more clear for the first quarter because we just started to sell right now. But we are very happy with the performance and I think, in a short-time, you can show to our investors, how important Cielo started selling a POS.

Another thing is when you analyze the performance from the hunters, that we just started beginning of January. We are talking about 1,000 hunters and their performance, it is 2.5 times more than the normal performance that we used to have in the past. It show us that, it's very important to focus just on hunters and going to maintain the farmers taking care of the current customers that we already have. Okay?

Q - Craig Maurer {BIO 4162139 <GO>}

Yes, thank you for the color.

Operator

The next question comes from Mario Pierry with Bank of America Merrill Lynch.

Q - Mario Pierry {BIO 1505554 <GO>}

Good morning, everybody. Let me ask you a question here. Related to your guidance. You're guiding for net income to contract about 25% in 2019. At the same time, you showed a slide at the beginning of your presentation, the retail sales in Brazil. The growth rate is accelerating quite rapidly. So, my question was, if you can provide us with some more color on what's behind your net income guidance in terms of volume trends that you expect for the industry and for yourself. Also you mentioned right, that the strategy here is clearly focused on market share and not on margins.

So can you give us a target market share, that you are trying to get to clearly, this is an industry that has seen a lot of changes, Central Bank trying to promote competition in the industry. so when we look back, we think it's natural for Cielo to be losing market share, your market share has declined from roughly 50% to 45%.

So I'm just trying to understand, at what level of market share are you going to be happy with. Thank you.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Thank you for the question. First of all, if we need to be involved in this kind of game, we need to go to the market and try to reach the market share, the market prices. In this case, we decided to focus on market share, because we need to maintain our leadership in this situation. The price, as I told you before, will be defined by the market, it's impossible to define this right now. But we are very concerned about our leadership, to remain in our position nowadays, as 45% in terms of market share, but doesn't matter for us, if we increase your -- decrease, a little decrease, because we are more concentrating this case to be the leader.

But to be involved in all of the segments and we believe, if you would be more involved in the micro entrepreneurs and the SMEs, we are going to have more scale and we're going to have more results. in this case, we believe that our strategy is focused on to reduce the results right now, but to be sustainable to be involved with the next steps that we will face in this battle.

Q - Mario Pierry {BIO 1505554 <GO>}

But Caffarelli, like the idea here is 45% market share, you are the leader of 42% market share, you still think you are the leader. So what I'm trying to get to -- is there a target market share or not really and how do you see this industry evolving as well. How many players, do you think at the end of the day, when things normalize or are we going to see in Brazil ?

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Mario, just one thing, related to this. It's very important to be the leadership okay. Cielo has more than 24 years. We were the first company to open the capital. In this case, for us nowadays the most important thing is to come back to the game, okay. Before we were a little bit concerned about March -- March, March. Nowadays, the fight is going to be in terms of to dispute the customer.

And if we have not been prepared for to face this, we can have some trouble in the future for us to maintain this. But as I told you before, there is no guidance for us. Now all, we need to follow to reach 40% to 45%, it doesn't matter for us.

The most important thing is to remain to maintain our leadership and to be competitive among the peers in this kind of market, because when we analyze this, perhaps the best company that can support the -- all those competitiveness that we have nowadays.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay and --.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

I think that, Victor would like to add something.

A - Victor Schabbel {BIO 17149929 <GO>}

To be clear, and following what Caffarelli said here. There is no clear target in terms of market share, but you are right, when you asked about, oh, you can be the leader with maybe 30% something, or 40% something percent of the market. You are right, when you mentioned that. The problem is that -- we here at Cielo, after losing so much in terms of share over the last two [ph] years. We cannot afford anymore, losing much more share and allowing other important competitors coming and becoming strong enough to compete neck-to-neck with us.

So that's why scale is important, that's why the focus is on paving the way for the growth to come again so -- and the volume growth, we will only come after we can have our client base growing again with the POS base growing further, so the volumes can be captured. So probably in the very short-term, before we can have our volume growth, accelerating, getting close to the volume growth that the market is posting, we should still see some short-term pressure on the market share.

But given the fact that we cannot afford losing much more, it's important for us to react fast and react now in order to avoid all the new player should come and become relevant, as some of the new players that are out there already became right. So we need to put some extra pressure and make the lives of everyone more difficult in order to show that the game is totally different. Right.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay . And can you share with us your outlook for the industry growth in 2019? So what are you expecting on your guidance?

A - Victor Schabbel {BIO 17149929 <GO>}

Closing detailed information about our guidance because we do believe that this information is strategic. You have out there some, let's say entities associations talking about the growth of the industry and we are obviously monitoring it. Definitely the market should grow quite well this year, but we are not going to disclose our specific expectation neither for the market, nor for us.

We are already providing the bottomline guidance for people to be on the same page but we are not going to -- disclose the strategic data at this point.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay. So my final question then is related to, in the third quarter you announced several new initiatives in order to add service to your clients right, you announced a QR code technology, also you introduced this POS terminal coupled with a phone. Can you just discuss with us how successful these strategies have been if clients have seen the value of these products ?

A - Victor Schabbel {BIO 17149929 <GO>}

Sure, Mario. These initiatives are very important for us to have the broadest portfolio possible. For us it should be serving clients in all the different segments, for example, the QR code is soon going to become more relevant in e-commerce. For example, we needed to develop the digital account for us to be effective in the micro entrepreneurs segment and so many others initiatives that we recently announced.

These initiatives are very important for the success of accompanying the medium to the long-term. In the short-term, we have been seeing, according to the surveys that we have been carrying-out that the clients are currently more sensitive to prices. Once prices are adjusted downwards, and the price that the merchants have to pay to accept payments become in their views more reasonable then we believe that product differentiation, service differentiation and clearly customer satisfaction will play bigger roles.

Because of that, in order to anticipate this new trend we are investing now at the same time that in the short-term, we are lowering prices. So we are not giving away the investments in products in differentiation because we do believe that soon at some point in the medium to the long-term these services, solutions, products will be effective in terms of adding value to customers. At this point however, in the very short-term, prices are more important for the customers.

Q - Mario Pierry {BIO 1505554 <GO>}

Okay, thank you.

Operator

Next question comes from Carlos Macedo with Goldman Sachs. Please go ahead.

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Q - Carlos Macedo {BIO 15158925 <GO>}

Thanks, good afternoon gentlemen. Couple of questions, first question related, it's more of a two-part question instead of one [ph]. Talking about pricing, obviously you adjusted your pricing as we can see the effects in the quarter, but it's not as if your entire client base, as you mentioned, the farmers out there, is now under the new pricing scheme. Conversely, when you look at the -- prepayment results that were delivered in the quarter, significant pressure on margins, on spreads that come from -- comes from pricing.

We know that, that business reprices quicker because the average term is around 40 days, 48 days. And so there is just a more opportunity for people to seek out better price. Based on that, on I was going to use a baseball analogy, but let's use a soccer analogy to make it simpler. How far along are you into the soccer game in repricing your client base. Are you 30 minutes into the first half, are you 15 minutes into the second half. How much more of pricing pressure, should we expect you to get over the next few quarters, as your entire client base moves to the new pricing scheme that you set out.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Carlos this is Caffarelli. I think that the game is just beginning. Okay. But the time of the game will depend on the markets, in this case I came to assure to you that we are prepared to be involved in this game. It doesn't matter, the time that will take place, we will expand.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. So just going back, then. Your spread declined by almost a third in your prepayment this quarter.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Okay.

Q - Carlos Macedo {BIO 15158925 <GO>}

Is that something that we should expect to be similar, for your take rate? Or is it a different dynamics there and it won't be that severe of a price-cut.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

It would depend, because I think, that when you analyze our relationship with our customers, nowadays you need to mix MDR, rental or sell-in prepayment. Okay. In this case, it will -- we can have some different strategies relating to the other segments, if we analyze it in terms of the -- large corporates, for instance. Perhaps the discussion is going to be just in terms of MDR, but if you analyse in terms of SME, S is happy nowadays. We need to be more aggressive in terms of prepayment because the -- our competitors, working hard in terms of -- to reduce price, relating to the prepayment.

Q - Carlos Macedo {BIO 15158925 <GO>}

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Fantastic. Final question. This may be a little bit more of a long-term question. Your net margin hits 24% this quarter, it's about -- it's the lowest it's ever been. And understandably you're focusing on volumes and rather than margins. Do you see room down the road for this margin to expand, maybe is there a new equilibrium for the market. And at that point, could your margin expand given operational leverage or will all the gains in margin be competed away, what's the company's view of that, that possibility.

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A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

I think that Carlos, considering that we are just starting to be more aggressive in the SMEs, perhaps we can have a best results in terms of March. When you're analyzing this, the end of the first quarter. Our performance comparing with our currently performance, because if you can increase SMEs and to maintain the corporates and the large corporates, perhaps you can increase our mix. This is --.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay. So --.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

This is that we wait to happen.

Q - Carlos Macedo {BIO 15158925 <GO>}

Okay, perfect. Thank you, Caffarelli.

Operator

The next question comes from Alex Spada with Itau BBA, please go ahead.

Q - Alex Spada

Hi, gentlemen, good afternoon. I have a couple of questions on the POS business. So first one, after what we have mentioned in the call in Portuguese, a good chunk of the number of terminals sold in this quarter, related to a very aggressive Black Friday campaign. If I'm not wrong, the number may be closer to 200,000 [ph]. It seems that if the number is true, if we exclude this campaign, the run rate of terminals sold on a per-month basis was not much different from the run rate of the previous quarter.

With that in mind, I just want to understand from you, what can we expect, as a run rate in terms of terminals sold per month or per quarter going forward. Now that we have all of these moving parts of Stelo and now the Cielo terminals that will be sold as well. So what are your expectations in this front.

A - Victor Schabbel {BIO 17149929 <GO>}

Thanks Spada. Thanks for the question.

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You are right, we have been very, we were very aggressive during -- the last Black Friday. The idea is to continue to be very effective and aggressive. Soon more investments in marketing will help us boost or keep boosting the sales of Stelo. But one important thing to be highlighted here is the pace, the growth pace of sales is accelerating is doing very well.

Unfortunately, we don't have Black Fridays, every quarter. But definitely we do have all the efforts here of our team, our partnering banks, ISOs in order to distribute more devices. So we will keep being very aggressive there. But one thing for you to take note, as well is the fact that the volume growth has been extremely relevant. Right. If it were only to be for the devices sold during November, we wouldn't have the spike that we had in the fourth quarter in terms of volume expansion.

So we have been growing sustainably through Stelo and this was not only a fact of a one-time event, one-time campaign. The results were already coming, obviously that we aim at getting more, that's why we are strengthening the efforts there down at the low-end with Cielo. Right. So Stelo was the beginning. Right. Stelo a brand that is less-known in the market started to do a very aggressive campaigns -- in order to start being recognized, in order to start growing with the support of the partnering banks and now a much more well-known brand like Cielo is joining the party. Right.

So that's why we should expect the growth down there at the low end to accelerate as well in the coming quarters.

Q - Alex Spada

Okay.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Alex. Just to add one thing that we talked before, if we add 5,000 branches from Banco do Brasil, 5,000 from Bradesco, more 5,000 from Caixa. We have a lot of spread around the country. I think, that will have a differential competitive, that you can be very involved in terms of to sell machines to sell POS from Stelo, even Cielo as well.

Q - Alex Spada

Okay, that's very clear. Thank you. And if you allow me a follow up, now that you'll be selling terminals, with the brand Cielo. Do you believe there could be some sort of an acceleration in cannibalization effect, considering the number of leads terminals that you still have in your base.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

I think that, you are right. But in terms of cannibalization, no, because it's different kind of POSs, even in terms of prices. Our -- sellers from, that are out of that Cielo selling machines. And our partners in Banco do Brasil, Bradesco, Caixa and other banks, they can have the both portfolio to offering, for offering to our customers. It's a little bit different, because Stelo always going to be less priced than Cielo.

Q - Alex Spada

Okay, thank you very much.

Operator

Next question comes from Jeff Cantwell with Guggenheim Securities. Please go ahead.

Q - Jeff Cantwell {BIO 18876343 <GO>}

Hi, good morning. Thank you for allowing me to join this calls and thanks for answering my questions. I appreciate all the color and any information you're providing with it, most of my questions have already been answered. But I want to ask you one on something you touched on earlier, on how you're changing your business model and those impacts on your margins.

So you're clearly saying you're at the beginning of a more aggressive commercial strategy with your pricing in order to acquire most SMEs. So if you look at your results, you've taken 8 basis points of pricing actually, this quarter versus last quarter. So, -- as we contemplate that dynamic, my question is, do you think, your commercial strategy is going to drive such a significant amount of new volume growth and new financial income that it eventually produces stable and maybe, expanding profit margins over the longer-term.

I just want to make sure, that's the correct medium-term, long-term expectation. If there's anything there that you can share with us in terms of how you're thinking about this in terms of timing, that will be great. Thanks.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Sure. Thanks, Jeff, for the question.

Well, first let's talk a little bit and discuss the background of our industry before entering to the medium to long-term trends for it. We came out from an industry that was organized in -- based on maybe two biggest exclusivity agreements, two monopolies or a duopoly, if you might classify like that 10 years ago. So now the industry became open for competition. The number of acquirers skyrocketed in just a few years. So we have over 20 acquirers registered at the Central Bank over 200 sub-acquirers, intermediaries operating the country as well. So we had a big expansion due to the high-profitability, the high margins that the industry had. It's natural now that after some players became viable, became relevant in our industry, new entrants that were successful, that there would be a reaction by the incumbents and also by the new entrants that were successful, reducing due to competition.

The returns that we were getting the margins, right. And this is exactly where we are, it's the beginning of this process. We are adjusting the returns, this should drive to lower margins in the medium-term. And after we have a more normalized scenario, we could once again, given the focus that we keep having on efficiency, maybe you start benefiting from increasing margins, increasing profitability in the future after the market goes

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through, this big fragmentation process that should be followed by some consolidation. Right.

So this is the expectation. After we have that maybe we could have margins improving and profitability improving again. In the short-term, this year maybe the next there should be still some pressure to be faced by us by the other players. And maybe after that we have a more normalized situation where the growth is back in scene. Margins start to recover and we have a more favorable reality for us and some of the others that would stay -- still be out there.

Q - Jeff Cantwell {BIO 18876343 <GO>}

Okay, that's very clear. Thanks very much.

Operator

The next question comes from Neha Agarwala with HSBC. Please go ahead.

Q - Neha Agarwala {BIO 17722501 <GO>}

Thank you so much for taking my questions. And thank you for the detailed answers so far. I have three questions, the first is on the prepayment business. So we see that the prepayment volumes have grown and they're now about 18.5% of the total trade volumes. Where do you see this going in the coming three, four years? We assume that, now that you're selling more to the smaller clients, this ratio, this percentage should grow. Any color on that would be very helpful.

The second is on the POS renting versus selling. Is it right to expect that over the next three, four years, we would have more of your clients asking to buy the terminals rather than renting it. And you would see some of your existing clients, who currently rent asking to buy the terminals instead. And the third is on the dividend payment, we know that you aim to pay about 70%. We had very good payout in 2018. What is the expectation for 2019 and what is the sustainable level of payout that you see in the medium to long-term. Thank you so much.

A - Victor Schabbel {BIO 17149929 <GO>}

Thank you for the questions, Neha. I will talk first about the prepayment trends and then about the POS and then I will hand to Caffarelli to talk about the dividends. Well, first about the prepayment penetration that we saw increasing now during the quarter. This is something that we want and believe we can keep posting going forward. So gradual increases in prepayment penetration once we increase exposure to smaller and mid-sized merchants, not to mention the increasing exposure that we naturally are going to have in the micro entrepreneur segment.

So we are not going to provide any specific guidance on that, but the expectation -- the belief that we have here at the company, is that the prepayment penetration should go up further in the coming quarters, leveraging on this better mix, and also leveraging on

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the new regulatory developments or recent regulatory developments that allow the acquirers to be more exposed to the receivables. Right.

In terms of the POS, if the sale of POSs is going to -- let's say, replace or become more relevant than the rental, it's hard to just say that in two, three years time, we are going to see a huge shift in terms of the scenario that we currently have. But what we can say is that there is clearly different demands, depending on the segments we operate at. For example, at the low end, clearly, you have to explore the sale of devices right and this is very true for the micro entrepreneurs.

When you move up and you start talking about medium-sized merchants, the rental does make sense because the rental is now way cheaper than it was a few years ago. The client has no problem, has all the supports coming from the acquirers, so he doesn't need to bother about the maintenance, replacing the device. So it's a service that is embedded on the rental, right.

So it depends maybe there will be extra pressure on the rental, but maybe this is not the client that will be aiming at buying devices. He clearly doesn't want to have this problem in his hand. So that's it, maybe the sale of the devices sold become more relevant in our POS base just because the micro entrepreneur segment is growing faster.

While the SME segment continues to rent, most of the devices but the growth there is less, let's say, relevant or significant than what we could have, at the low end.

Now I will hand you to Caffarelli to -- for the dividends to be discussed.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Before, dividends just to add one thing relating to the rental and sales devices. It's important to reinforce that we are discussing about different kind of customers. In this case, there are a lot of customers just focused on rental. And, there is more customers like sub-entrepreneurs, we are talking about rental. In this case, we can establish this kind of difference, okay? In terms of prepayment, I think, that we can have a very specific situation in Brazil, considering that the penetration in terms of credit card industry, is less than 30% of the total of the transactions.

I believe that if we analyze, as Victor said before, relating to the Banco Central, the regulator rules and the new customer that we will acquire for the next two [ph] years, we can have a lot of opportunity to be involved in terms of prepayment and other kinds of anticipation related to the receivables.

Relating to the payouts, the dividends, we established that the dividend is going to be from 70% up to 100%, it will depend in their performance around the year. And during the year, we will define which percentage, we will pay, but we will start with 7% right now that you can reach to 100%. Okay, thank you, Neha.

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Q - Neha Agarwala {BIO 17722501 <GO>}

Thank you so much.

Operator

This concludes today's question-and-answer session. I would now like to turn the call back over to Mr. Paulo Caffarelli to proceed with his closing remarks. Please go ahead sir.

A - Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Okay, thank you so much for the participation. If you have some doubts, please do not hesitate to contact us, to contact our department from Investment Relation and we are ready for -- to be responsive in terms of our strategy. Okay, thank you so much and have a good day. Bye-bye.

Operator

This concludes the Cielo conference for today. Thank you very much for your participation and have a great day.

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