

Q1 2013 Earnings Call

Company Participants

- Eugenio Mattar, COO
- Nora Lanari, IR
- Roberto Mendes, CFO, IRO
- Salim Mattar, Chairman, President, CEO

Other Participants

- Asher Hochberg, Analyst
- Irma Sgarz, Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good morning. Welcome to the First Quarter 2013 Conference Call of Localiza Rent A Car. Hosting the event today are Mr. Salim Mattar, Chairman of the Company's Board of Directors; Mr. Roberto Mendes, Chief Financial Officer; and Nora Lanari; Investor Relations.

We would like to inform that the numbers in this presentation are state in millions of Brazilian real and based on US GAAP until 2010 and based on IFRS from 2011 on. The presentation will be recorded. And all participants will only be able to listen to the conference call during the Company's presentation.

Immediately afterwards, we will start the Q&A session for analysts and investors when further instructions will be provided. (Operator Instructions). The audio of the conference call and accompanying slide presentations are being broadcast simultaneously over the internet at the address www.localiza.com/ir. The slide presentation can be downloaded at the same address by clicking on the banner 1Q13 Webcast.

Before proceeding, we would like to clarify that any statements made in the conference call concerning the business outlook of the Company forecast as well as operating and financial targets represent the opinions and assumptions of the Company's management which may or may not occur.

Investors must comprehend the economic conditions and other operating factors may affect the Company's future and may lead to materially different results from those stated

in this call. I would like now to turn the presentation over to Mr. Roberto who will begin the presentation. Please, Mr. Roberto, you may now begin.

Roberto Mendes {BIO 7289124 <GO>}

Good afternoon, everyone. And thanks for attending our conference call. In the First Quarter of 2013, economic activities continue to grow at a moderate level, reflecting on lower growth (inaudible) volume. The market continues to expect a historic pace of growth in the second half with a GDP growth of 3% in 2013.

Investments in the new concessions announced by government show leverage such growth. (inaudible) in a lower growth base scenario, the (inaudible) in market pressures in the expresses with (inaudible) and we state (inaudible). Company presented our record net income in this quarter and the total invested capital was kept stable in 15.1%.

We will be even straighter on constant control to maintain margins even with the potential of lower growth of economic activity. (inaudible) to its comfortable cash position in financial stability, the Company was well-positioned to take advantage of growth opportunities for an economic exploration expecting for the next quarter. And to present First Quarter results 2013, I will turn the floor to the head of IR, Nora Lanari.

Nora Lanari {BIO 18838335 <GO>}

Good afternoon, everyone. And thank you for attending our conference. On slide number two we present some highlights of the First Quarter 2013. The Company presented a record net income of BRL88.8 million, 22.1% growth compared with the First Quarter 2012. In the spread between ROIC and cost of debt after taxes presented a 1.8percentage point growth which is 9.8percentage points.

On slide number three we presented growth evolution of the car rental division. In First Quarter 2013, rental base grew 2.9%, reflecting the weak performance of economic activity. Net revenue presented the growth of 5.7%, mainly due to this growth in rental volumes, an increase of 3% in average rental rates.

GDP growth expectations through the acceleration of infrastructure investments are welcomed by the car rental division.

On the next slide, slide number four, we present the evolution of car rental location. In the First Quarter of 2013, four rental locations were added to the Brazilian network. And five locations in South America, Localiza's system current holds 533 locations in nine countries where the Company operates.

On the next slide, slide number five, we present the volumes of end revenues of the fleet outsourcing division. In First Quarter 2013, net revenues in the division grew 9.5% leveraged by the growth of 5% in business volumes. And 3.8% in average rental rate.

In the next slide, number six, we present the fleet net investment evolution. By maintaining a higher pace of car purchasing in First Quarter 2013, fleet was only reduced by 585 cars compared with 4,562 in First Quarter 2012.

On the next slide, slide number seven, we present end of period fleet evolution. Localiza ended the quarter with 96,255 cars, a 5.3% growth compared to the First Quarter 2012, including franchisees fleet, Brazil and abroad, fleet total 111,000 cars.

Slide number eight presents the evolution of SemiNovos stores. Used of car sales network supports the business model of the Company allowing direct sales to (technical difficulty) maximizing the generation of cash for fleet renewal. In the First Quarter of 2013, one store was opened for sales of the commission cars for fleet renewal.

And slide number nine presents consolidated net revenues evolution. In the First Quarter of 2013, consolidated net revenues grew 2.4% due to the increase of 7% in the rental revenue from both car rental and fleet outsourcing division. SemiNovos revenues, on the other hand, was reduced by BRL10 million due to a 2.6% decrease in the number of cars sold, an effect of OEMs delay to deliver cars at the end of last year, resulting in a decrease of the cars decommission for fleet renewal.

With the increase of cars available for fleet renewal at SemiNovos, sales volume grew from 3,900 cars sold in January to 4,000 cars in February and 5,000 cars sold in March.

In slide 10 we present EBITDA evolution. In the First Quarter of 2013, EBITDA totaled BRL270 million, 3.4% higher than the same period last year. In the First Quarter, car rental division EBITDA margin was impacted by car purchase volumes reflecting in higher mobilization cost, such as licensing and freight. And was also impacted by the increase in personal and real space expenses.

The Company remains with its credit adjustment maintaining car rental rates stable aiming at market consolidation as long as it does not compromise the target expressed. Even considering that some effects were non-recurrent, the Company has been strongly acting on cost reduction aiming at maintaining margins similar to 2012.

The lower EBITDA margin in the First Quarter was offset by the lower basic interest rate. And the return on invested capital was capped at 15.1%, stable when compared to the First Quarter of 2012. In the fleet outsourcing division EBITDA margin remains stable at approximately 66%. SemiNovos EBITDA margin of 5.6% reflects the conservative position of the Company in calculating the depreciation adjustment as for the IPI tax reduction for new cars.

And the fleet purchase before the IPI reduction is renewed. SemiNovos EBITDA margin shall return to a normal level of 2%.

Let us now move to slide number 11 where we present the average depreciation for cars in car rental and fleet outsourcing division. As for the government of IPI tax extension on

May 2012, the Company adjusted its fleet depreciation to reflect lower market value of its cars. In the First Quarter 2013 average generalized depreciation per car in the car rental division was BRL1,274 and in the fleet outsourcing division it was BRL5,427.

On March 30, government reduced the maintenance of the IPI reduction for new cars until December 2013. Such announcement does not bring any additional impact on the Company's car depreciation since the additional depreciation accounted as for the reduction announcement was calculated over the entire fleet of the Company. Such decisions were based on the parameters that the car crisis would not return to IPI reduction levels even when the tax was reinstated.

On slide number 12 we present additional depreciation due to the IPI tax reduction for new cars. The table shows the recording of additional depreciation of BRL180.5 announced to reflect the impact of the tax extension for new cars in the market price of all of SemiNovos cars. In the car rental division, 98.6% of the additional depreciation has already been recorded.

In the fleet outsourcing division 62.2% was accounted and the remainder value will be diluted within the next two years. In the First Quarter of 2013, the average additional depreciation recorded was BRL10 million.

On slide number 13, we present the net income evolution. In the First Quarter of '13, the Company presented a record net income of BRL88.8 million, 22.1% increase compared to the same period last year. Even after recording the 10 million additional depreciation expense mentioned before. Net income increase occur due to the BRL7.2 million EBITDA increase added to the BRL2.6 million decrease in financial expenses, partially offset by increases in car depreciation, income tax. And social contribution line.

Slide number 14 presents the free cash flow in the First Quarter of 2013. This quarter, Localiza presented a free cash flow of BRL76.6 million, even after reducing the car supplier's accounts by BRL56.7 million.

On slide number 15 we present the changes in the First Quarter of 2013 debt. This quarter net debt was reduced by BRL37.7 million, or 3.1%.

On slide number 16 we present the debt amortization profile. Company is still presenting strong cash position and comfortable debt profile.

On the next slide, number 17, we present debt ratios which reflect the financial discipline of the Company. Company's prepared for the growth opportunities leveraged by the strong economic activity.

In slide number 18 we present the spread between the ROIC and the cost of debt after tax. Spread remains flat at 9.8 (technical difficulty). Mattar for consideration about his succession.

Salim Mattar {BIO 7288067 <GO>}

Thanks Nora. Good morning, all. On the next slides, 19 and 20, we present the current structure of the Company's management and its new structure as after May 2013. Five years ago we had started a process of preparing my succession. Eugenio Mattar, my brother and one of the founding partners, COO of Localiza is ready to step up to the CEO position from May 1st.

Eugenio has been working with me throughout those four years, financial department was always been under his responsibility. One of the strongest components of Localiza recognized by the market for its conservative strategy. He was responsible for implementing the fleet outsourcing business, but of which and also for implementing the new business model of used car sales, SemiNovos Localiza.

As the CEO, having care rental division under his responsibility, the largest business of the platform. He has demonstrated a strong abilities in market and the process, all of that, subject to his respected leadership and his clear human resources vision, (inaudible) a well prepared objective to take the CEO position.

After 40 years, leaving the business, I will lead the CEO position under Eugenio's responsibility and the opportunity of director of the board. I believe we will be celebrating a welcome (inaudible) succession process adding value to the Company.

As executive chairman of the board, I will be here working fulltime and will be making my best effort to better perform my new responsibility, with the growth of the Company, leveraged by the new challenges in the future opportunities, it is imperative to have an active board of directors to add even more value to the Company. Furthermore, like of the Company's governing principles, the Chairman and CEO position should not be occupied by the same person.

As you all know, we have a professional board with four definite members who have a deep knowledge in business, strategies, financing, marketing, retail. And international market. (inaudible) is considered bench market in the Brazilian market.

In slide 21, we separated the specific functions of the Chairman, the CEO. And the shared functions of both positions. As Chairman of the Board, I will have the role of represent Localiza before society to define corporate governance standards, to guide and defining the mid and long-term strategies and to promote the execution on new business models and portfolios.

Eugenio, in his CEO position, will continuously seek innovation and improvement on our management model. Deploy strategies integrals (technical difficulty) and play Localiza's Executive role as CEO before press, investors, market. And employees. Shared functions between both position are the launch to manage the value through shareholders. To (inaudible) institutional crisis, strategic planning. And to review your goals business possible to guard the culture and the values of Localiza.

Eugenio and I believe in this new restructure. We reaffirm our strong commitment to the Company and confident that this change in the structure will allow Localiza to become even more competitive, focused on adding value to the shareholders and prepared to be the consolidator on the Brazilian fragmented car rental markets.

Let's now move to the Q&A session.

Questions And Answers

Operator

Excuse me ladies and gentlemen. we will now begin the question and answer session. (Operator Instructions) And our first question comes from Mitza (inaudible) with Bridge Capital.

Q - Unidentified Participant

Hi, guys. Hi, Salim. Congratulations on a very successful tenure. We'll miss you but I know you won't be going very far and you'll be there. My first -- my question is for Eugenio, I hope he's on. But I'm curious to know what he -- where he thinks the big areas to generate incremental value specifically on the car rental side? Is it on pricing? Is it on volumes? Is it on margins; and how he's thinking about that business specifically?

A - Nora Lanari {BIO 18838335 <GO>}

Mitza, I'll turn the floor to Eugenio to answer the question.

A - Eugenio Mattar {BIO 3986664 <GO>}

Hi Mitza, as well a pleasure to be here with you all guys. Car rental division nowadays. And this year we have a little pressure by the market because of the low of the economy. And we are putting pressure on all our segments. We are working with as airport and downtown. And we are putting a lot of push in the cost to reductions also. This was more of maybe a proposal because of the perspective of the low ball of the economy.

A - Nora Lanari {BIO 18838335 <GO>}

Adding a little bit Mitza, in that sense, we are not willing to increase prices this year. We will maintain the strategy of holding on to rates in order to maintain the competitiveness of the Company as long as we are able to maintain the stress and the ROIC. If you see the figures from the First Quarter of this year, ROIC was capped at 15.1%, the same level of the First Quarter of 2012 even with the pressures and the margins.

So the main value addition here might come from volume and from the initiatives of the Company in cutting costs.

Q - Unidentified Participant

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Bloomberg Transcript

Okay. And my next question is Salim, we're you still going to be doing budgeting. And selling. And negotiations. And that stuff; or is that responsibility somebody else's?

A - Salim Mattar {BIO 7288067 <GO>}

Hi, Mitza, thank you for the question. For (inaudible) lost time, it may be up to the end of this year. Eugenio and I both will continually (inaudible) negotiated with the auto makers. But I believe that I have new responsibilities. I need to leave this function to Eugenio, maybe from January of 2014.

Q - Unidentified Participant

Okay. Okay. Great. Well, congratulations and all of that to you guys.

A - Salim Mattar {BIO 7288067 <GO>}

Thank you, Mitza.

A - Roberto Mendes {BIO 7289124 <GO>}

Thank you.

Operator

Our next question comes from Ms. Irma Sgarz, Goldman Sachs.

Q - Irma Sgarz {BIO 15190838 <GO>}

Hi, thanks; and congratulations again. I just had one follow-up question from my earlier from the Portuguese call and I was curious to see where would you see -- there was a lot of focus in the earlier question and answer session about the cost control that you would put in place as it would be focused on in order to offset the inflationary pressures and the lower growth environment and obviously potentially also the highest selic rates. And I was curious which areas in the Company do you think are still offering opportunities for cost control and for more efficiency gains? Thank you.

A - Nora Lanari {BIO 18838335 <GO>}

Irma, thank you for the question. As mentioned in the Portuguese call, we told that we are not willing to cut cost in terms of personnel. Okay. So in that sense we have opportunities in all business areas. But I would say current opposition is one important area in terms of fixed cost. It's tough to manage a strong decrease in personnel and the lead of our rental location. So we will try to work on many lines as we can, except for personnel. We will pretty much look for cutting cost in every other line.

Q - Irma Sgarz {BIO 15190838 <GO>}

So just if you -- if I may following up there. So you are saying that on leases it's probably hard -- I guess it depends on when leases are coming up for renewal. And what would some of the other areas be? Is it marketing, or is there something that is specially -- that you can specifically -- any line that you can specifically point to? Thank you.

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A - Nora Lanari {BIO 18838335 <GO>}

Market is -- marketing is one of them. In our supply chain line we are developing suppliers to service all around the county. And by guarantee volumes we may guarantee discounts. So we have a number of initiatives. It's -- we will not go into all of them here. But marketing is one. You are right. Suppliers are another important line that we are working with.

Q - Irma Sgarz {BIO 15190838 <GO>}

Thank you.

Operator

(Operator Instructions) And our next question comes from Irma Sgarz with Goldman Sachs.

Q - Irma Sgarz {BIO 15190838 <GO>}

Yes. Thanks for giving me another opportunity. You were alluding also earlier on the -- on your opening remarks in the earlier call to opportunities for productivity gains. So to drive additional growth above and beyond what's provided by the market. Are there any examples that you can provide where you see that these productivity gains can be realized? Thank you.

A - Roberto Mendes {BIO 7289124 <GO>}

Irma, to grow (inaudible) one of the investor you're probably (inaudible); but everything that you can -- is possibly out of productivity. For example, if there some operators decide to not work anymore, probably you're not replacing this one. This kind of thing you can do more with less people. It's just an example, to give you an example. But every thing you've been involved more in fixed costs.

A - Nora Lanari {BIO 18838335 <GO>}

Another example we can give you, Irma, is the IT investments that have been done in the last years to increase the productivity of our process. So we are reducing the needs of personnel and we are automizing most of processes; it's another initiative here in the Company.

Q - Irma Sgarz {BIO 15190838 <GO>}

Helpful, thank you.

Operator

Our next question comes from Asher Hochberg with Crestwood.

Q - Asher Hochberg {BIO 19763697 <GO>}

Bloomberg Transcript

Hi, Nora. Just a quick clarification question on the SemiNovos EBITDA margin; you mention it's going back to 2%. Is that only after the IPI tax cut is eliminated? Or is that something that happens nonetheless? And my second question is the BRL1,300 for car depreciation in the car rental division? If you'd run the accounts forward. Thank you.

A - Nora Lanari {BIO 18838335 <GO>}

Thank you, Asher for the questions. As a matter of fact we believe SemiNovos margins should be growing towards the 2% (technical difficulty) this year, the second half of this year. And the reason is because (technical difficulty) it's likely too conservative in forecasting the residual values of those cars when the IPI tax cut was announced. So we ended up selling cars slightly above what we anticipated. So in the moment we started to renew the fleet.

Or we end the fleet renewal of those cars. But with the IPI tax we should see this margin conversion to the 2%. So throughout 2013. On regards to your next question, please repeat it.

Q - Asher Hochberg {BIO 19763697 <GO>}

The depreciation per car for the car rental division is about BRL1,300 on the annualized basis. Is that a good run rate going forward to the next remainder of the year?

A - Nora Lanari {BIO 18838335 <GO>}

Yes. As a matter of fact market is expecting a number between BRL1,300 to BRL1,400 for the full year.

A - Roberto Mendes {BIO 7289124 <GO>}

Just to add (inaudible) in the second half, probably (inaudible) deal model, 2014 model. So because there is probably the depreciation behind the second half, it's now excluded the additional depreciation around BRLBRL1,000. So BRL1,000. So it's not the normal level. The normal levels, it's from the full year leverage years, BRL1,300 or BRL1,400 level.

Q - Asher Hochberg {BIO 19763697 <GO>}

Okay, thank you.

Operator

Our next question comes from Mitza with Bridge Capital.

Q - Unidentified Participant

Hi guys, it's Mitza again. I had a question on your free cash flow on your balance sheet, if you look at the market is slower than, or weaker than anticipated. You should be generating a lot of free cash flow because you won't be going with fleet very much. And your balance sheet is at a level that it's really ever been and that's the lowest that it's really ever been and the cost of that is also the lowest it's ever been. So I'm curious how you're

thinking about that going forward. But do you generate non-free cash flow in a slow year. If we get the same environment this year, you'll be running an even lower than '13. So how are you thinking about balancing that going forward?

A - Roberto Mendes {BIO 7289124 <GO>}

Okay. In fact we are in a cash (inaudible) market we generate a lot of cash. So our net debt is decreasing. And (inaudible). In the second half of this year probably we were thinking about it and how to -- we can do with this cash in our hands. But now the first half we will not do anything. We will just wait -- what will happen with the GDP if the (inaudible) growth of GDP is not just 1%. We will move to three or more. Yes. We need to expect a deal to do something.

A - Nora Lanari {BIO 18838335 <GO>}

Mitza, adding to your first question in regards of free cash flow generation, you have to remember that you paid BRL56.7 million in car OEM supply this quarter. In the sense of the deleveraging of the Company you were right, it is still too early for us to think in changing anything in terms of cash distribution because we believe in the growth of the Company for the figure. So as Roberto said, it is still too early. Let's see how economic activity will play out in -- throughout 2013 for us to work better on that.

Q - Unidentified Participant

Okay. Great. Thank you.

A - Nora Lanari {BIO 18838335 <GO>}

Thank you.

Operator

(Operator Instructions) This concludes today's question and answer session. I would like to invite Ms. Nora Lanari to proceed with her closing statements. Please go ahead.

A - Nora Lanari {BIO 18838335 <GO>}

I would like to thank you all for attending our conference and make our IR department available for any questions. Thank you.

Operator

That does conclude Localiza Rent A Car audio conference for today. Thank you, very much for your participation and have a great day.

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