Y 2020 Earnings Call

Company Participants

- Eugenio Pacelli Mattar, Chief Executive Officer
- Mauricio Fernandes Teixeira, Chief Financial Officer and Investor Relations Officer
- Nora Mascarenhas Lanari, Investor Relations Officer
- Rodrigo Tavares, Chief Financial Officer
- Unidentified Speaker

Other Participants

- Alexandre Pfrimer Falcao, Analyst
- Julia Toledo, Analyst
- Lucas T. Barbosa, Analyst
- Nathan Churchill, Analyst
- Regis Cardoso, Analyst
- Rogerio Araujo, Analyst
- Stephen Trent, Analyst
- Unidentified Participant
- Victor Mizusaki, Analyst

Presentation

Operator

Good afternoon and welcome to the Localiza Rent a Car Conference Call of the Fourth Quarter of 2020. Hosting the event today are Mr. Eugenio Mattar, CEO; Mr. Rodrigo Tavares, CFO; and Ms. Nora Lanari, Investor Relations Officer.

We inform that the numbers in this presentation are stated in millions of Brazilian reais and based on IFRS. 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 conference call, audio and the accompanying page presentation are being broadcasted simultaneously over the Internet at www.ir.localiza.com/en. The page presentation can be downloaded at this same address by clicking on the banner 4Q20 webcast.

Before proceeding, we would like to clarify that any statements made during the conference call concerning the business outlook of the company, forecasts, as well as operating and financial targets represent the opinions and assumptions of company management, which may or may not occur. Investors must comprehend that political and 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.

To start to fourth quarter of 2020 teleconference, I'll turn the floor over to the CEO, Mr. Eugenio Mattar.

Eugenio Pacelli Mattar {BIO 3986664 <GO>}

Good afternoon and thank you all for your presence. In 2020, we faced enormous challenges in our businesses, but once again we prove our resilience and adaptability, planning and execution. In the context of the pandemic, we acted quickly. In March, we established our crisis management committee which handed important results on five main fronts: care for our employees, our customers, our operations, our liquidity and society. We instituted the remote work policy and a new methodology to foster and measure team productivity, engagement and management during this period.

We're able to see that our employees were who inspire and transform once again proved their role and boldness in building the future of mobility. We took care of our partners and society around us, reinforcing our role as a company committed to citizenship. We contributed with approximately BRL16 million initiatives to support the healthcare system including hospital infrastructure and equipment as well as in actions with small and medium businesses strongly impacted by the pandemic and vulnerable citizens.

We made the right decision to reinforce our cash with new funding instead of accelerating the reduction of our fleet in the period of low liquidity in car sales. Thus we saw the increases in new car prices passed through to used cars resulting in smaller depreciation during the second semester, notably in the last quarter of 2020, the challenge became the temporary limitation of the capacity to expand fleet through the acquisition of new cars due to the reduced supply of vehicles in the national market forcing us to reduce the pace of selling used cars in Seminovos.

We are confident that setbacks and challenges in the automotive supply chain will be resolved with the restoration of production and supply levels along the second quarter of 2021. Even in rough seas with the reinforcement of the structures, and the right decisions we kept our planning for the future and continue to invest in important advances. It's worth mentioning the launch of local lease vehicle, a new way of having a car that presents a long-term subscription mobility model for individuals and small and medium-sized companies. We created Localiza Labs, Localiza's technology and innovation laboratory with around 700 professionals, which leads our digital transformation, increasing our capacity for internal development of new solutions.

We also looked around us and through careful choices we took important steps. We acquired Mobi7, which brings us several opportunities for fleet monitoring, telematics and internet of things. We are connecting the entire fleet at a fast pace while adding several functionalities for our operation, our business and our customers. We also announced the combination of operations with you need us a transaction that can be transformational for the rental industry and generate a lot of value for all stakeholders.

2020 was for the Localiza team a year of great boldness and protagonist. The challenges demanded resilience, flexibility and a lot of agility to make the right decisions, which contributed to the quick recovery of volumes and prices allowing the delivery of record results. We surpassed the BRL1 billion net profit mark. This performance is a result of a solid culture that is strengthened with the evolution of time supported by a base of great trust and ethics.

Last year we mentioned in our letter about the strong changes that the world of mobility was going through, without having at the time the visibility of the effects that quarantine and social distance due to the coronavirus pandemic, could have in accelerating this process. Today we have the perception that changes in habit should further accelerate the adoption curve for new technologies and innovations in mobility. We seek these opportunities generated by

Cultural and social change and we are absolutely focused on continuing to serve our customers with pleasure and fulfilling their needs in this environment of constant change.

In the past few years, our market has expanded considerably and Localiza the protagonist in this expansion is the company that has the best service and solutions to the demands whose origins are the most diverse. And this diversification makes our business highly resilient, adaptable and attentive to trends, allowing us to direct our efforts to the best opportunities in the market.

For the country, we contributed significantly with more than 11,000 direct jobs and collection of BRL723 million in taxes net of credits in addition to approximately BRL1.1 billion in taxes on the purchase of cars. In addition to this is the movement and promotion of an entire ecosystem of multiple businesses that involves from large industries to thousands of SMEs and service providers spread across all regions of the country.

This year that inspired us even more to take care of others, we evolved in our attention to diversity, an extremely relevant topic for the Company, with initiatives that include the launch of Diversity Inclusion Program. We have a mission to work continuously towards a respectful plural environment that instigates creative and constructive debate for both our business and society.

On the environmental front, we made significant progress in neutralizing emissions from our operations for the year of 2019, reported in the 2020 emission inventory, and we became partners and supporters of the Commitment to the Climate Program, a movement with the purpose of engaging and inspiring the private sector in climate responsibility actions. In 2020, we were honored with the recognition by several communication medium and inclusion in international rankings for our investment in initiatives in the three pillars of ESG.

To continue building the future of mobility, we maintain our focus on generating value and having a positive impact on society, our customers, and partners. We continue to invest in the improvement of our processes and of our customer experience, valuing long-term relationships. We know that great challenges were overcome, but we are aware that others will come and will bring on new opportunities, which we will be prepared to embrace with boldness, innovation, and agility.

Yesterday at the end of the day, we also announced my succession. I'm going to be the Executive Chairman, working full-time in the company, supporting Bruno Lasansky, who was -- is going to be my successor as a CEO. He is absolutely prepared to take on my position and to steer Head Localiza for the upcoming years in a well-organized and planned process. And in a way to preserve the experience of those who join us and the renewal with the new person that joins us. So, continue working together with Bruno as the CEO and our Chairman will be the Vice President of the Board of Directors in the next mandate. Thank you.

Now I'd like to hand over to our CFO, Rodrigo Tavares.

Rodrigo Tavares {BIO 21760011 <GO>}

Thank you. Eugenio. Good afternoon, everyone. It's with great pleasure to inaugurate my presence as CFO in Localiza's earnings conference call and share with you the 2020 results of the company this closing record results.

Starting on Page 2, we can see a summary of Localiza's operating highlights for 2020. In Car Rental, we reached the average rented fleet of over 156,000 cars in the fourth quarter consolidating the resumption of volumes with the growth of 4.1% year-over-year. The division ends the year with a volume growth of 8.9%. The fourth quarter of Car Rental was marked by high utilization rates and tariffs, a result from efficient fleet management and pricing in the context of vehicle unavailability. The utilization rate reached 84.5% in the quarter reducing the impact caused by the pandemic in the second and third quarters of the year and 73.5% in the year, while the average daily rate was BRL79.6 in the quarter and BRL68.5 over the year.

In Fleet Rental in 2020 we had an increase of 11.7% in the average rented fleet, reaching more than 59,000 cars. Quarter-over-quarter, the average daily rate in Fleet Rental grew 0.7% and in the year-over-year it increased 2.3%.

On Page 5, we can see the financial highlights for the quarter and the year. In the quarter, consolidated revenue falls 2.2%, reflecting the company's decision to curb sales of used cars in the context of lower supply of new cars, but with a 19.5% growth in EBITDA.

While in the year consolidated net revenue grew 1.1% reaching BRL10.3 billion and EBITDA increased 11.5% driven by a lower depreciation quarterly EBIT grew 56.6%, while annual EBIT exceeds BRL1.8 billion with an increase of 21%. We achieved record quarterly and annual profits exceeding BRL400 million in the quarter and BRL1 billion in the year.

To present further details on fourth quarter results, I'd like to hand the floor over to our Investor Relations Officer, Nora Lanari.

Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Good afternoon, everyone. Thank you Rodrigo. Giving a little more detail about the results of the quarter and of the year, I would like to start with the Car Rental division and would like to highlight that from this earnings release, we now report the Franchising division together with the income statement of the Car Rental division. So that the numbers presented on Page 4 already reflect this change.

Going on to the highlights, in 2020 the average rented fleet of RAC grew 8.9%, an increase of more than 11,000 rented cars on average in the year. Net revenue increased 3.2% when compared to the previous year. In the fourth quarter, the revenue growth was 12.1% year-over-year, exceeding the mark of BRL1 billion in revenue in the quarter, mainly due to the average daily rate practiced in the period.

On Slide 5, we see that the average daily rate of BRL79.60 in RAC increased 10.4% compared to 4Q '19 reflecting in the efficient management of the mix and prices per segment and the utilization rate achieved 84.5%, the result of an efficient fleet management in the context of scarcity in the availability of cars, which remains in the first quarter of 2021.

On Page 6, we show that the network of own branches was expanded by 15 units compared to the end of 2019, of which six were branches previously operated by franchisees. In addition, several branches have been expanded or renovated to increase their capacity and enable fleet expansion.

Moving on to Slide 7 in the Fleet Rental division, the average fleet grew 5.1% and net revenue increased 7.7% compared to 4Q'19. In the same comparison, the daily rate rose 2.3% mainly reflecting the pricing of new contracts that reflect higher car prices and expansion of the Localiza Meoo which broader mix with a higher rate. In the year the Fleet Rental division increased by 11.7%. The average fleet and 12% in net revenue, which totaled more than BRL1 billion.

Moving on to Slide 8, we show the balances of car purchases and sales. During the year despite having delivered volume growth both in Car Rental and Fleet Rental, we reduced the fleet by 26,000 cars. The investment in the 2020 fleet achieved BRL5.5 billion and the net result of the fleet reduction was a generation of BRL585 million. In the quarter, we bought 42,748 cars and even in a period of strong demand for used cars, we reduced the decommissioning pace and sold 31,857 cars to enable an increase of almost 11,000 cars in the current context of lower offer of new cars.

Referring to what we currently see, in the beginning of the year we point out that the automakers are working on restoring production levels and shipping volumes, but the context of restriction still remains with the supply chain affected by the pandemic.

On Slide 9, we show the Seminovos network. In 2020 we opened seven new stores. In the quarter we limited the volume of cars sold by reducing the decommissioning pace, working with a smaller number of cars available for sale and thus prioritizing Car Rental during the high season. As a result, we had a volume of 31,857 cars sold, a drop of 23%, partially offset by the strong increase in the sale price of 15.7% in the quarter, reflecting the increase in the price of new cars. We ended the year with 130 points of sale and 135,490 cars sold.

On Slide 10, we show the end of period fleet, which was reduced by 9.6% with over 292,000 cars, a reduction of 9.2% in Car Rental and 10.6% in Fleet Rental. The reduction in the end of period fleet as already mentioned was offset by the higher rate of views of cars with the average fleet rented in both divisions growing in the year.

Moving on to Page 11, we see that the consolidated net revenue for the quarter decreased by 2.2% year-over-year. Net rental revenue increased by 11.1% in the quarter while that of Seminovos' dropped 10.9% due to the reduction in sales volume, partially offset by higher prices. In the year, consolidated net revenue grew by 1.1% when compared to 2019. In 2020 net rental revenue increased by 5.3% being 3.2% in the Car Rental Division, and 12% in the Fleet Rental Division. In Seminovos net revenue decreased by 1.6% when compared to 2019 due to the 8.4% drop in sales volume offset by the 7.4% increase in the average price of cars sold.

Moving on to Page 12, consolidated EBITDA increased by 19.5% in 4Q20 compared to the same period last year as a result of the higher margin in used cars and the expansion of revenues in the company's business divisions. The EBITDA margin of RAC falls forth 0.3 percentage points compared to the margin of the fourth quarter of 2019. Considering the same basis, especially due to the recomposition of leadership salaries that had been reduced in the period that the company adopted the government program to support employment due to the increase in tax provisions and allowance for doubtful accounts, and increase in the provision for part profit sharing reflecting a better than expected annual result for the year in the context of the pandemic.

Fleet Rental had a margin reduction of 2.6 percentage points mainly due to the recomposition of salaries and the provisioning of profit sharing as described for RAC. Seminovos' presented a margin of 10.1%, continuing the effect of the substantial increase in prices practiced in the sale of used cars which reflect increase in new car prices. The higher price levels should maintain a higher level of Seminovos EBITDA margin in the upcoming quarters when we will still be decommissioning the vehicles purchased at lower prices. In 2020 consolidated EBITDA was close to the BRL2.5 billion mark, showing an increase of 11.5% when compared to 2019.

On Page 13, we show the evolution of depreciation. As a result of the expectation of increase in sale prices of cars and the fleet, as a consequence of the general increase in prices practiced in the market. In the fourth quarter, we see a 48% drop in the RAC depreciation and in relation to the 3Q20 reaching BRL612 per car. In the year, the average annual depreciation per car reached BRL1,707 a decrease of 11% when compared to 2019.

In the Fleet Rental division, the average annual depreciation per car was BRL1,907 in the fourth quarter, 17.5% lower in relation to average depreciation in 3Q20. In the annual comparison, there was a drop of 44% in the average annual depreciation per car, which is mainly explained by the change from the SOYD method to the linear method for calculating depreciation in addition to the increase in sales prices.

On Page 14 we can see that the consolidated EBIT in 4Q20 reached BRL645.4 million representing a 56.6% growth compared to the same period last year due to the 19.5% increase in consolidated EBITDA combined with the decrease in the depreciation of cars. The EBIT margin of the Car Rental division was 46.7%, representing an increase of 14.6 percentage points compared to 4Q19 especially due to the reduction in depreciation and to the used car margin.

In the Fleet Rental division, the EBIT margin was 63.4%, representing an increase of 15.1 percentage points compared to 4Q19. In RAC especially due to the reduction in depreciation and the used car margin. In 2020, the Car Rental Division, EBIT margin was 35.1% representing an increase of 1.4 percentage points compared to 2019. In the Fleet Rental division, the EBIT margin was 66.4%, an increase of 17.3 percentage points in the same comparison.

Net income for the fourth quarter on Page 15 grew 75.9% year-over-year, reaching BRL401.8 million. The expansion of net income is explained by the growth of EBITDA of approximately BRL123 million combined with the reduction of depreciation of approximately BRL114 million and financial expenses of approximately BRL47 million partially offset by the increase in taxes on profit of approximately BRL107 million. In 2020, the company had a record accumulated profit of BRL1 billion representing an increase of 25.7% in relation to 2019.

On Slide 16, we show the cash generation before the fleet reduction of BRL1.3 billion in 2020. The reduction of about 26,000 cars in the fleet generated about BRL1.2 billion used to reduce the balance of accounts payable to automakers.

As can be seen on Page 17, there was an important generation of cash from rental activities, combined with the generation cash from the reduction of the fleet, partially offset by the reduction in the level of accounts payable, interest expenses, repurchase of shares and payment earnings resulting in a reduction of net debt by approximately BRL500 million in the year.

I would like to turn the floor back over to Rodrigo.

Rodrigo Tavares {BIO 21760011 <GO>}

Thank you, Nora. You can see that on page 18 we ended 2020 with the debt profile that will help in the resumption of the growth path post-pandemic and cash position of almost BRL4 billion. We continue to actively manage the debt profile.

On Slide 19, we can see that the net debt over a period of ratio ended the year at 2.5 times the lowest leverage since 2016. We consider that a comfortable level to expand and finance growth without the need for equity in the short-term considering our leverage policy and environment of low interest.

To conclude, I would like to highlight the evolution of the annual consolidated ROIC spread versus the cost of debt that can be seen on Page 20. In 2020 the year in which we had to face all the setbacks generated by the pandemic, we delivered a nominal spread of 7.4 percentage points higher than 2019 generating value for our shareholders in an extremely challenging year. We maintain our goal of delivering profitable growth and we will leverage our competitive advantages to capture business opportunities and continue to develop and expand the car rental market in Brazil.

Before I conclude on Page 21, we have our advances and sustainability with the evolution in the three dimensions. We are now open to answer your questions.

Questions And Answers

Operator

Ladies and gentlemen we will now begin the Q&A session. (Operator Instructions). The first question is from Alex Falcao from HSBC.

Q - Alexandre Pfrimer Falcao {BIO 5515455 <GO>}

Good morning, everyone. I have two questions actually. The first one is about the used cars dynamics, I'd like to understand if what's happening is a decrease in the spread between the new cars and the used cars and the fact that there are practically no new cars available in the market and when there is new cars available again the spread will come back or is it inflation and the new car prices raised a lot. So the dynamics that we saw in the fourth quarter should continue for at least a relevant period. And the second question is about subscription cars. I'd like you to talk about the size of that business and the perspectives for that and if you have a relevant bet in relation to that. Is the competition focusing on that as well. Talking about that, will that eventually be modeled in a different way in the future. And I'd like to know where you think that business will be in the next two years or five years that would be very interesting. Thank you.

A - Unidentified Speaker

Thank you. I'll answer first about the spread between the new cars and used cars and then Nora can add in relation to the subscription cars. What we've seen is not a compression of the spread of the new car compared to what we can sell the used car for. We see historical levels of that difference. What actually happened is that the new car prices have gone up because of the exchange rate, lack of inputs and transferring that cost increase and that has been transferring to used cars. But we don't see a compression in the spread.

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Falcao, thank you for your questions. About subscription vehicles, we launched Localiza Meoo on September 22 and right after that we went into the context of the restriction of new car supply given that long chain of inputs for the automakers. So it's really hard to give you some exact numbers about the run rate for that business, but we're pretty optimistic about the product, the perception has been very good and so is the demand. To start, we don't have the idea of breaking that down into a sub-segment as we don't with RAC.

Q - Alexandre Pfrimer Falcao {BIO 5515455 <GO>}

I'd like to follow up on the depreciation policy. Given all of that's going on and new cars prices are still going up. Do you think that you would decrease depreciation given the car price dynamics or will depreciation eventually be adjusted? Apparently, it was a scenario last year and now in the new scenario if it stays that way. Will it still drop?

A - Mauricio Fernandes Teixeira {BIO 19758664 <GO>}

About depreciation, we have to assess the seasons. So the cars that were bought before the pandemic, that had a different price before the new car price increase then you see that already depreciated with low depreciation for the new cars that are being added to the fleet come in with the new prices. So the depreciation policy that we always have is the expectation of price realization and the expectation of going back to normal levels in buying those new cars.

Composition of depreciation will receive the interference from this two car seasons, so to speak. The older cars and the cars that were recently bought. And Falcao, I'd like to add, I know that we are in during a period of restriction of car we receive so, it's becoming 100% depreciated. We have more cars getting close to zero depreciation. So I'd say it's two things, the first part, you have lower depreciation for these cars as we mentioned and as fleet renewal and we recompose the volume of delivery go up to average depreciation then you'll see an increase of the average depreciation.

And the EBITDA of Seminovos will only be reflected in the future because throughout the year we will sell the cars that have already been 100% depreciated and already have a positive margin. So the depreciation will go up throughout the year, but the EBITDA margin will still remain a bit higher for a longer period throughout 2021.

Q - Alexandre Pfrimer Falcao {BIO 5515455 <GO>}

Yeah, that was my next question. Okay, thank you.

Operator

Next question is from Lucas Barbosa from Santander.

Q - Lucas T. Barbosa {BIO 20835372 <GO>}

Good morning, Eugenio, Rodrigo and Nora. Congratulations on your results and thank you for taking my question. My question is related to one of the previous questions about receiving brand new cars. So you already -- I imagine that you plan to get a limited number of cars in the first quarter. But now, how do you see, in fact, what was actually delivered? Was it in line with expectations, any positive or negative surprises? And when do you think things will come back to normal and then I'll ask my second question. Thank you.

A - Mauricio Fernandes Teixeira {BIO 19758664 <GO>}

Thank you. Well the expectation for the first quarter was to receive less cars and it's within our expectations. So now we're waiting because, as beginning of the second quarter and if production goes back to normal, I believe vehicle supply will come back to normal.

Q - Lucas T. Barbosa {BIO 20835372 <GO>}

Okay, thank you. Second, is about the average age of the RAC fleet. So I'd like to understand what the strategy is for the next quarters. If you can have a higher average age as you will be selling more cars because of the peak of leisure would have passed.

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Lucas, thank you for your second question. Our business is Car Rental, it's not selling cars. So we will prioritize rental cars and fleet and if there is additional possibility of selling then we can slow down the volume of sold cars, which we did in the third quarter, we sold 45,000 cars and we can do more, but we slowed down to 30,000, thirty-some thousand in the fourth quarter. We base that on the demand of rental and then the receipt of new cars, that's how we base it on..

Q - Lucas T. Barbosa {BIO 20835372 <GO>}

Thank you. Nora that's clear. Good morning.

Operator

Our next question is from Rogerio Araujo from UBS.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Good afternoon, Nora, Eugenio and Bruno. Good luck to your new job position. I have two on my side. First on fleet rental. One of your competitors has been saying or has been showing actually that they are closing new deals and it's much higher than the fleet increase. So they've been accumulating a lot of contracted vehicles and just waiting for the vehicles to be delivered by the automakers to enter fleet. Is that also happening to Localiza? Have you been closing a lot of contracts and fleet rental, but we haven't seen that in your results because of the delay in car deliveries from the automakers? That's my first question.

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Thank you, Roger, for your question. During a crisis I believe that more companies will be outsourcing and they will cash in their own fleet and become a client. So we've seen that demand. But there is the context of restriction of car delivery and there is also this new path of the subscription cars. So we're confident that demand will continue to be, but it's not outside the regular standards.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Thank you, Nora. My second is about the ICMS tax provision that was done, I'd like you to confirm the number. It's BRL49 million in the cost breakdown, costs and expenses, but in the wording in the text, it says BRL68 million. So I'd like to know the provision for the ICMS tax and can you talk about the year-to-date period for that provision. So since when have you been is it a one-off provision will there be a cash effect and what's the impact moving forward. I imagine that there will be a new policy for ICMS payments. So what's the impact? What's the recurring impact in the next quarters because of that? Thank you.

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Rogerio, we mentioned some extraordinary effects that affected the margins, not only in car rental but also fleet during the fourth quarter. And one of them were the tax provisions. In note number 23, we have a breakdown and it differs from 17 because one part is booked above the EBITDA and the other one is under EBITDA because it's accounted for as financial expenses. So you have a BRL49 million impact to the EBITDA and the difference from the BRL68 million to the BRL49 million were booked as financial expenses. That's mainly a result of discussions in the last five years provisioned and as they're written off we reverse. Oh, I forgot, there is another part US moving forward right, moving forward we don't see that risk.

Q - Rogerio Araujo {BIO 17308156 <GO>}

Okay, perfect, very clear. Thank you very much and congratulations on your strong results.

Operator

Next question is from Stephen Trent from Citibank.

Q - Stephen Trent {BIO 5581382 <GO>}

Good morning everyone and thank you for your time. First of all, this is Steve Trent. First of all, my condolences on Roberto Mendes, he was an amazing person. I have two questions. Why did Mauricio to share a leave? Can you, I'd like to know for how long he was the CFO. It was a three or four years. Is that correct?

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Hi, Steve. Thank you for mentioning Roberto. Yes, we do miss him. About Mauricio, I think it's worth asking him as well. He was with us for about four years. He is an executive that we truly respect and admire and well seen by the market. As a personal decision, he decided to take on a new challenge and was announced as the CFO of Hep Vida. So it was a personal decision and he goes back to Sao Paulo and he is taking on a new project at Hep Vida. It was a personal decision and we truly respect him and admire him and our home is his home. So we have open doors.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay, thank you very much, Nora. Just one more question, please. Why is the spread between the ROIC and the cost of debt? Why did it drop from the third to fourth quarter and why -- is it because the invested capital increased?

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Stephen, we look at the third and fourth quarter of 2020, If I understood the question, the spread increases. So, but there are some ways to report that. In 3Q we reported nine months annualized and we broke down the third quarter annualized. So the spread annualized was 9.5%. In the fourth quarter report where we have 2020 closed which is the ROIC that you saw of 10.2% with a 7.4% spread, if we calculate the spread the ROIC spread fourth quarter annualized, the ROIC would have been 15.1%, so it's mainly because many competitors report in a different manner. So we want to have, to make this comparable. So our ROIC in 2020 was 10.2% with a 7.4% spread and the fourth quarter annualized would have been 15.1%, a spread of almost 12, 13 percentage points.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay, great. Thank you very much, Nora.

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Steve, I forgot to mention the last part of the question. The capital base has been increasing because the price of new cars is going up. Note that since the exchange rate devaluation and we saw a transfer of new car prices of 15% to new cars, and that has been impacting the price of the cars that we buy. And in Seminovos, we can capture the new car prices and we have a similar transfer to that price. So even though the capital base has increased depreciation dropped. So (inaudible) is better and we saw an evolution of ROIC every quarter throughout 2020.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay, I understand.

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

So part of it was the accounting interference in the period.

Q - Stephen Trent {BIO 5581382 <GO>}

Okay, I understand. Thank you.

Operator

Next question is from Regis Cardoso from Credit Suisse.

Q - Regis Cardoso {BIO 20098524 <GO>}

Hi, everyone. Good morning. Thank you for taking my questions. Congratulations on your results. Two more specific topics. First, figures and then more general. So the specific about figures, I want to talk about margin. So in the margin specifically, there is more than one subject actually, so we saw a margin reduction relating to cost and expenses given that the price has gone up and in cost and expenses, we already mentioned some, there was the ICMS provision.

Could you also comment on profit sharing provision and how much that impacted is it recurring or not. I'd also like to understand the comment about if there is going to be another cost increase in the fourth quarter because of the comeback of people after the COVID issues and then about expenses and costs. So in marketing expenses, I've seen that that's growing and in cost there is maintenance. I know it's a very long question. I wanted to number the effects. But I'd also like to understand what happened in costs and expenses that's putting pressure on the margin.

The other specific question is about the tax rate for this year, it seems like there is an issue about car depreciation because of IFRS and the OCP payment couldn't have been hired to improve the rate, so we can start off with that.

A - Rodrigo Tavares {BIO 21760011 <GO>}

Thank you, Regis, let me try to summarize the effects. If we look at the effects that we consider extraordinary for the fourth quarter, we have profit sharing obviously the expectation was in to achieve this result and when we have that expectation, we adjusted the amount and we also had the salaries, going back to normal, we already mentioned that and the removal of the Hertz brand from our branches. And if we combine all of these factors, I can say that that would impact the margin by 6.6 percentage points in Rent a Car and two percentage points in Fleet Rental or Fleet Management.

So there are extraordinary costs and they do affect the margin significantly and that explains a part of the reduction. Nora, would you like to talk about the tax, the rate?

A - Nora Mascarenhas Lanari {BIO 18838335 <GO>}

Regis just to remind you we have the depreciation that we report the 600 some per car and we have the tax depreciation that's used to pay taxes. So it's 20% linear in five years. The main reason for the income tax rate is related to interest on own capital. And since we have less profit throughout the year-end, interest on own capital is on a quarter, so we paid less than that and the taxable profit grew with less leverage, so it was network was growing, but our equity was growing with lower profits though. So the management proposed that in the shareholders meeting, the payment of BRL18 million in dividends to add to the minimum mandatory amount of 25%. So we don't expect that impact moving forward, there was an effect of profit volatility especially in 2Q20 given the pandemic.

Q - Regis Cardoso {BIO 20098524 <GO>}

Thank you, Nora and Rodrigo. I have a follow-up on costs. So two expense lines that are volatile in 4Q, marketing bad debt and maintenance. The fourth quarter is that recurring levels for maintenance and then on another note, there are two large avenues for growth, which is subscription cars and app drivers. I'd like to know if Localiza 2.0 has been helping you to increase your share even in a bigger horizon of drivers that you consider profile and credit. So is the new product is helping to mitigate the credit risk and the addressable market.

A - Unidentified Speaker

Thank you. Regis for your question. I believe that the marketing increase is a result of the high season, so more individuals and the sale of Seminovos in retail in a context when we are slowing down sales, we focus more on rental, but they do have a higher average rate, but you need more marketing efforts based on that. So bad debt was higher year-over-year. So in 4Q20 it was higher over 4Q19 but it's already showing a dropping trend.

"So 90 days", after the worst effect of the pandemic for the company and then you have a dragging effect from that, but it's already lower in 4Q over 3Q when we believe it will continue to normalize and go back to very historical low levels for the company. There are no evidences that it will remain high quite on the contrary after the pandemic is over. We believe that it will go back to more normal levels.

You mentioned subscription cars and then you mentioned the app drivers. Let me start off with the app drivers and then I'll understand your question what you want to know about Meoo. About incremental improvements in the product, we've been doing that across times on the app. We've been adding new features to the app and we believe that we'll get more granularity, more or less default rates. So I believe that we'll have benefits with these applications that are embedded in the app.

That said, we are in a context of car restriction, right. So we can't really say that there is a relevant change, but it should be a competitive advantage for Localiza as we implement it and we measure that by the net promoter score. So we have some measures of general customer satisfaction, we break that down per segment and per touchpoints that the customer has with us. About subscription cars, I got a little lost on that, I'd like to you to ask about that again.

Q - Regis Cardoso {BIO 20098524 <GO>}

Actually it's not really a specific question about the app cars and no worries about the subscription cars, it was just a general question, I'd like to know if you see that as an avenue for growth. Are those the two largest markets where you can grow your share? Those two, that's what I mean, if, increasing the addressable driver's scope. So, increase the scope of app drivers and the other was subscription cars because it's a market that competes with new car sales.

A - Unidentified Speaker

Okay. Regis. Thank you. We see the rental car market with low barrier of entry and a lot of growth, I wouldn't limit that to subscription cars or app cars. We have a low share in the individual segment. Even in the corporate segment, there is a migration of rental of owning a car to renting a car. So we still see a huge avenue for growth there in the most diverse segments that the company operates. So I wouldn't say that they are necessarily the biggest drivers.

Q - Regis Cardoso {BIO 20098524 <GO>}

Okay, thank you.

Operator

Next question is from Julia Toledo from Citibank.

Q - Julia Toledo

Hi, good afternoon. Congratulations on your results. And my question is that few foresee any impact of Ford leaving Brazil?

A - Unidentified Speaker

Thank you, Julia. Well of course it's very unfortunate that Ford is leaving the country, a centenary company. There is an impact on jobs, so it's bad news, not only for the automobile market for automakers. It's also bad news for the country. About the impact, we believe that it's a limited impact they already had a very limited small share of the market, which was 7% and given the idle capacity that the industry has that volume should be absorbed easier by the remaining players in the country.

Q - Julia Toledo

Okay, thank you.

Operator

Next question is from Victor Mizusaki, Bradesco BBI.

Q - Victor Mizusaki {BIO 4087162 <GO>}

Good afternoon, congratulations on your results. I have two questions. First one, Rodrigo when we see the slide that talks about leverage and debt profile, Localiza has a very comfortable position. I would like to understand if it would make sense for Localiza to use that flexibility to try to negotiate your working capital pay faster so to speed up the delivery process and now in the succession process, given the negotiation between the Localiza and Hertz merger, why not now or after the merger?

A - Rodrigo Tavares {BIO 21760011 <GO>}

About the first question. We use all the levers in the negotiation with automakers. So we always look at negotiation in a very holistic manner and if necessary, If we have to use the levers that enable us to have better conditions for competitiveness to purchase cars, we will use them and not only limited to liquidity. So we're always looking at the negotiation in a very complete manner and use everything that we have available to guarantee that we will have more competitiveness in cars. About succession, Eugenio would you like to comment?

A - Eugenio Pacelli Mattar {BIO 3986664 <GO>}

Good morning, Victor. Thank you for your question. Localiza has prepared a well-structured and organized succession plan. Bruno has already been the CEO of the company for a while, he really understands the business. So the company continues to act as an independent company. We won't be tied to future decisions of other instances. It was a process that would happen and now this is the right moment because I will remain in the company as a Chairman, Oscar as the current Chairman will remain as well. So there was no reason not for us to do something that was already mature to happen.

Q - Victor Mizusaki {BIO 4087162 <GO>}

Okay, thank you.

Operator

We have a question that came through the chat, I'm going to read it from Rodrigo (inaudible). Rodrigo, thank you for your question. Good afternoon, Eugenio, Rodrigo and Nora. Congratulations on your results on such a challenging year. I have two questions, please comment on this strategy and execution and the prioritization of the segments in RAC and the strong tariffs in the fourth quarter. Are the rates offering a yield in line with the increase of brand new cars or were you able to leverage a rate that was even better.

A - Unidentified Speaker

Rodrigo, thank you for your question. We took advantage of the high season of the summer vacation in Brazil this October, November, December and January and given the context of a restriction of new car supply, we were very selective in our mix of the segment. To offset the "lack of cars". So we had to use a utilization rate higher reaching 84.5% and increased the weight of the mix of individuals, which is a mix that usually -- a profile that usually rents more during summer vacation. So that said, the mix in relation to 2019, compared to 2019 is still closer to the longer-term segment and lower rates. So the mix doesn't explain the yields gain, it was a selective pricing that we had in relation to the fleet. And a part of that increase helps to offset the increase in car prices, but we still have to see the increases that we will have in 2021 given the context of the transfer of steel costs and we still have scarcity in the supply and the automakers are still getting back to speed.

Operator

There is a second question, with the increase of the average age of fleet, does that impact the service level and a reduction in RAC rates to offset that?

A - Unidentified Speaker

The company is very careful in quality of service for our customers. So obviously the fleet is aging. But we under -- the cars undergo maintenance and prepare the cars and undergoing a supplies scarcity. So, we'll price accordingly. So in the first quarter, the peak of summer vacation drops and historically we have a comeback in the long-term segments. So that could reflect the average rates will see throughout the quarter.

Q - Unidentified Participant

The previous was from Rommel. Bruno leave it now. Good morning, everyone. Could you give further detail about new car delivery by the automakers last year with there were delays in deliveries? I'd like to know if that gap was normalized or if that still close to happen?

A - Unidentified Speaker

Last year there was a restriction in supply, especially in the fourth quarter and restrictions continue. In relation to the volumes that were offered in the fourth quarter, those were already delivered in 2021. So new volumes that were negotiated. There is still a lot of uncertainties and we're waiting for gradual normalization in 2Q, but especially in providing the semiconductors. That's the main issue. So we expect normalization from 2Q on, but there are still uncertainties that we can't be sure of.

Operator

We have one last question here on the chat in relation to the ESG Initiatives, what are the plans for 2021 to continue the incredible environmental, social and governance performance.

A - Unidentified Speaker

Well, thank you very much for the price and the question. We will continue, we do plan on advancing it on all fronts in relation to the sustainability. The company always has the perception of strong governance that was always perceived. In the past three years, we've done relevant efforts on the social and environmental side and we will continue on that trend of evolution.

Operator

(Operator Instructions). We have a question in English from Mr. Nathan Churchill from American Century.

Q - Nathan Churchill {BIO 3667017 <GO>}

And I was wondering if you could help us understand how we should be thinking about the margins in RAC in particular in the context of the extra costs that you just had this quarter. So if there were some 600 basis points of added costs, should we anticipate that any of that carries into 2021?.

A - Unidentified Speaker

Thank you for your question. I'm going to answer your questions. So the extraordinary costs we see them as non-recurring and they shouldn't affect the year 2021. Obviously, throughout the year, there should be other expenses and costs that we haven't planned, but those specific ones that have the fourth quarter in 2020, we don't expect that there will be an effect in 2021.

Q - Nathan Churchill {BIO 3667017 <GO>}

Thank you.

Operator

We have one more question on the chat. What will your general work, would be like in the company's day-to-day with this change?

A - Eugenio Pacelli Mattar {BIO 3986664 <GO>}

Thank you for your question. I will act as the Executive Chairman, meaning a Chairman, that will be fully dedicated to the company. I'll be handling future plans. I will support the CEO in his activities, I'll be considering the company's strategy, acting strongly in governance and ESG and I'll be a coach for the CEO, while he taking on his new position and focus on the institutional side of the company.

With the class associations, our act on the institutional matters related to the industry, work with the with Unidas and the process with the Brazilian Antitrust Agency with CADE, not much an operational focusing mainly on the strategy of the company, working with the CEO to guarantee that the standard of governance and culture and investments in ESG are coherent and in line with our proposal and purpose.

Operator

Now I'd like to hand back over to Mr. Rodrigo Tavares.

A - Rodrigo Tavares {BIO 21760011 <GO>}

Thank you very much for your presence. Our IR team is available for any further clarification. Have an excellent day.

Operator

The Localiza Rent-A-Car conference call is now over. Thank you for your participation and have a good afternoon.