

Q1 2021 Earnings Call

Company Participants

- Gustavo Henrique Santos de Sousa, Executive Vice President - Finance and Investor Relations, Member of the Executive Board
- Paulo Rogerio Caffarelli, Chief Executive Officer, Member of the Executive Board

Other Participants

- Jeff Cantwell
- Neha Agarwala

Presentation

Operator

Good afternoon, everyone and thank you for waiting. Welcome to Cielo First Quarter of 2021 Results Conference Call. With us here today, we have Mr. Paulo Caffarelli, Gustavo Sousa and Danielle Denise [ph]. This event is being recorded and is also being broadcast live via webcast and maybe accessed through Cielo Web site ri.cielo.com.br/en/ where the presentation is also available.

Participants may view these slides in any order they wish. The replay will be available shortly after the event is concluded. Remember that the participants of the webcast will be able to revisit via website questions to Cielo that will be answered soon.

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

Presentation published for this morning on the company's website, this conference call is open exclusively for question and answers. (Operator Instructions).

Now, I pass it to Mr. Paulo Caffarelli for opening remarks.

Paulo Rogerio Caffarelli {BIO 7429811 <GO>}

Thank you. Thank you all for joining us today. As you see we have changed the conference procedures just for optimizing the meeting here together with you today in the morning.

We provide the speech in the presentation on our site. It's available over there. And now we are going to the Q&A. Thank you. We can go to the first question.

Questions And Answers

Operator

(Question And Answer)

Our first question comes from Jeff Cantwell, Guggenheim Securities.

Q - Jeff Cantwell {BIO 18876343 <GO>}

Hi, thank you for taking my questions. Can we go down a little bit into the cadence that you're seeing in payment volume right now? I guess what we're trying to understand is, maybe you could give us a sense of the trajectory coming out of March into April and what might be reasonable to anticipate, over the next call it six to nine months, any color you can give us there would be great? Thanks very much.

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

Hi, Jeff. Gustavo here. Thank you for your question. Well, first of all, let me please ask you and the participants that if you want to follow-up on the comments that I'm going to make, please take a look at Page 4 from our presentation there you'll see the TPV from Cielo that's the second graph, second chart in the top, where you see the year-over-year growth of TPV.

As you can see, we started the year with a January and a February that were as close to normal as one could expect given the pandemic. However, given the increase of the impacts of the COVID in the Brazilian economy in March, we felt a decrease of TPV in March. So far Jeff, in April, we are on a similar trend on what we given what we saw in March, April is on a similar path, which is lower than January and February in terms of TPV for this year.

It's hard to forecast what we're going to see in terms of activity in the next month because it has everything to do with economic activity given the impact of the COVID in the country, okay. But I can give you some color on what happens, what is related to the impact of COVID on TPV. So what we saw in March and we also see in April is a lower TPV versus the beginning of the year, but also a shift of concentration of activity in larger clients.

We also saw that on the months that were most impacted by the pandemic crisis last year, whenever we have an increase impact in the economy, we see a concentration of volume in larger accounts. Naturally, those larger accounts have a lower margin.

We also see a concentration on debit cards, we see an increase in debit cards participation versus the historical trends. So Jeff, I'm sorry to not answer your question

directly, because it's very hard for me to point out what's going to happen in terms of economic activity. But I can tell you that what we've seen in April is similar to what we saw in March, both in terms of lower volume, and also a concentration in debit in larger accounts, okay.

Q - Jeff Cantwell {BIO 18876343 <GO>}

Yes. That's very helpful. And I understood maybe as a related follow up to that. Is there any discussion right now about mix and the reason that I ask is, if we look back to last quarter, the past several quarters, you've been very consistent in terms of moving strategically into the SMB, portion of the pyramid.

And what we're trying to do is put together what the mix and try to anticipate what mix might look like, over time, given all these different macro-economic and strategic variables that we're trying to contemplate right now. So if there's any kind of color you could give us there in terms of mix impacts, as you're anticipating them going forward? That would be great as well, thanks very much.

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

Thank you for that, Jeff. You're correct. Our absolute focus is on SMBs. That's why we added 500 new employees to our sales force. And that happened late December and also in the beginning of this year. It is our aim to reach a balance in our TPV of 50% of larger accounts and 50% of SMEs plus entrepreneurs.

Given the impact of COVID in the economy and the increase in participation of large accounts, when that happens, it's hard to say if we will be able to achieve that this year, but it is our aim to achieve a balanced portfolio, 50% of large accounts and 50% of the other segments, okay?

Q - Jeff Cantwell {BIO 18876343 <GO>}

Understood. And then, my last one, and this is in reference to Slide 3 of the presentation. Can you tell us a little bit about the WhatsApp partnership? I guess, I'm trying to figure out to what extent you can talk about that in terms of customer base for Cielo?

Does it open up that buy back funnel and increase your addressable market for your customer base? Should there be a certain mix of volume that you can sort of foresee at this juncture? I know, it's very early days, but maybe could you talk to us a little bit about that partnership and give us a little bit of color? That'd be greatly appreciated.

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

I have to talk in very broad terms, Jeff, because Cielo is a service provider for WhatsApp. And WhatsApp is the face before the Central Bank, right. So what we have received is an approval for the transfers, possibilities -- transfers function in WhatsApp.

What we are still waiting approval for is for the P2M transactions. Once we get there, we will have a great offering for our client base over a million clients that can use this

functionality. But so far, that's all I can say I can't talk because we're still pending regulatory approval for the P2M function of disagreements with WhatsApp. There's not a lot that I can say in terms of timing and the impact of that, okay.

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

Gustavo, if that may add something. The question is we are evolving in both situations in B2B solutions and P2M between as well solution. We got the authorization from Banco Central. Related to B2B and we hope that soon perhaps next month, you can start with the B2B solution.

Cielo is supporting WhatsApp, Facebook pay in these services, okay. And perhaps till the end of the year in the second semester, we can have the authorization related to the P2M. It's important to reinforce that the P2M there is no --, Cielo, perhaps we will start with these kinds of services. But in fact, we can have the other competitors together with us.

The main thing that was -- we were selected only us, we were selected by the WhatsApp, Facebook and now perhaps, we can have another kind of competitors and another kind of acquires together with us in these services. But it's impossible from now to establish some kind of revenues related to this, because you don't know when we start with the P2M solution. Thank you.

Q - Jeff Cantwell {BIO 18876343 <GO>}

Okay, thanks very much. Appreciate it.

Operator

(Operator Instructions) Our next question comes from Neha Agarwala, HSBC. Excuse, Ms.Neha your line is open.

Q - Neha Agarwala {BIO 17722501 <GO>}

Sorry, I think I was mute, can you hear me now.

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

Yes.

Q - Neha Agarwala {BIO 17722501 <GO>}

Okay. Thank you for taking my questions. Given your focus on the retail segment and especially the middle market, the SMB clients, how would you compare the products, the wide range of products that Cielo has, as well as the service offerings of Cielo with your main competitors in this segment? And then I'll go to my next question.

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

Hi Neha, Gustavo, here. Thank you for your question. Well, I'm going to try to split my answer in two. So on the traditional acquiring products, we have a very competitive

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offering, we have a complete portfolio of equipment, products and pricing for our clients, okay. What we are expanding on and we made a point about that in our presentation is in our value added services. Specifically this quarter, we talked about in our presentation, our investment in convertible debentures -- which is a company dedicated to servicing the restaurant market.

We also announced an agreement with Google and better ads to provide services for our SMBs. We went over this on the last question, which was, WhatsApp received the approval from the central bank for the transfers function. And we also did in agreement with Payface for face recognition payments and also in agreement with Focus Energia, which is an energy company in Brazil to offer energy contracts with a lower price for our client base. So both in traditional acquiring products and in value added services, we have a competitive offering and still expanding in value added services.

Q - Neha Agarwala {BIO 17722501 <GO>}

This is very clear. But given the fact that most of the acquirers are now offering the working capital credit as well to the merchants, do you think that is the factor in a merchant choosing, you are not choosing you in the offering?

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

I don't think that's the key points for choosing an acquirer, but it is definitely an important product and one that Cielo will expand on. We'll talk about this product and the development of that in upcoming quarters. But it is a product of strategic importance and Cielo is developing a competitive alternative for its clients.

Q - Neha Agarwala {BIO 17722501 <GO>}

Okay. I believe you have been looking to diversify taking MeS, anything that we can expect in the short-term regarding MeS?

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

Neha, what I can say about that is that for the third consecutive quarter MerchantE has presented an improvement in its bottom-line. If we look at MerchantE standalone, the operation company and not Cielo USA, which is a holding company that has the investment and MerchantE, but also the bond that was issued to finance that investment.

So if we look at MerchantE alone, again for the third consecutive quarter, we have an improvement in performance and they are very close to breakeven, even with an important impact of the COVID in the American economy in the first quarter and also still with some restructuring costs at MerchantE. What I can tell you is that MerchantE is at the very end of the turnaround process that we have designed alongside management over there, okay.

Q - Neha Agarwala {BIO 17722501 <GO>}

Understood. Last question I want to touch upon is, is the agreement with Caixa? You mentioned that TPV is over 5% of total Cielo's TPV. And you mentioned that there are

some rebates that you paid to Caixa which you don't have to pay anymore?

Could you give us more sense of the impact on your income statement from this agreement with Caixa? And how are you trying to retain these clients that you currently serve? And who are Caixa's clients?

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

Thank you for the question, Neha. So I'm sorry to give you a broad answer, but it's important to clarify a few points about Caixa. Okay, so first of all, I cannot get into the details of economics with Caixa because our agreement with them, which is still a valid agreement has clauses about commercial confidentiality.

As I said in the Portuguese conference call Caixa has over 5% of Cielo's TPV. And Caixa is the fourth bank in terms of volume inside of Cielo. So and when we talk about those four banks, inside of Cielo, naturally, two of them are controlling shareholders that have commercial agreements with Cielo just like Caixa.

And one of them is another big retail bank in Brazil, but that does not have a contract with Cielo, that demonstrates that Cielo given its size and presence throughout the country has a fair share of acquiring it with any given bank in the country.

We believe that currently we do 50% of the acquiring that is done for Caixa clients. When a competitive process such as this one that Caixa ran right now happens, we have a player, such as Cielo that is already working with those clients, they have to be very mindful of how it's going to bid, because we have volume to gain. But the price for the volume to gain is increased share of economics.

And what we stand to lose is how much of this acquiring client base we are going to lose if we are not successful in that bid, given that we already had 50%, given that we believe that we have two relationships there. We have the banking relationship and we have the acquiring relationship for a lot of those clients, we have been their acquiring partner for years. We believe that Cielo is well positioned to keep providing acquiring services for those clients.

And actually what happens, the only automatic thing that happens when such a change occurs is that when the contract expires, we will start paying commissions for Caixa. Those commissions will translate into temporarily and increase let's say bottom-line for Cielo and this increased bottom-line can be transferred to clients to have a more competitive offering for them.

So this is how we look at developments regarding our relationship with Caixa, a value partner, but we have developed the acquiring relationships with that client base as well.

Q - Neha Agarwala {BIO 17722501 <GO>}

Perfect. And can you just tell us when does the contract expire so that you can stop paying rebates?

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

We are still waiting on the notices related to that, we know that there was one successful bidder, the next steps are still pending.

Q - Neha Agarwala {BIO 17722501 <GO>}

So should be in the coming months. Not too long.

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

I would expect that.

Q - Neha Agarwala {BIO 17722501 <GO>}

Okay. Perfect. Thank you so much for those answers and thank you so much for your time.

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

Thank you Neha.

Operator

(Operator Instructions) This concludes today's question-and-answer session. I would like to invite Mr.Gustavo to proceed with his closing remarks. Please go ahead, sir.

A - Gustavo Henrique Santos de Sousa {BIO 17683157 <GO>}

Thank you everyone for participating. I hope you have enjoyed this format of submitting the presentation with the video and the audio beforehand so that the market has more time to elaborate the questions. So we will follow up with you to see if you have any suggestions for the next quarter and Cielo and its IR team are available for any questions you may have. Thank you very much.

Operator

That does conclude Cielo conference call for today. Thank you very much for your participation and have a nice day.

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