

Q2 2017 Earnings Call

Company Participants

- Jose Antonio de Souza Azevedo, Chief Financial & Investor Relations Officer
- Luis Fernando Memória Porto, Vice Chairman & Chief Executive Officer

Other Participants

- Renato Hallgren, Analyst
- Álvaro Frasson, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning. Welcome to the teleconference for Locamerica, where we will see the results of Q2 2017. Right now, all the participants are connected only in the listen mode. Later on, we will have the Q&A sessions, when we will supply more information.

In this quarter, Locamerica will also have space for press professionals, right after the market analysts. This teleconference has simultaneous translation into English in progress. Questions may be asked from listeners from abroad. You can also send questions through the Web.

We'd like to remind you that this call is being recorded. The audio will be available in the company's site in up to 24 hours. If you don't have a copy of the release, you may obtain it in the company's website, www.locamerica.com.br-ri. This teleconference, together with the slide presentation, is being transmitted simultaneously through the Web and also accessed through the company's website.

Before we continue, we'd like to say that any declarations made during this call, concerning the business perspectives of the companies and also projections and goals concerning the growth potential are based on management's expectations concerning the future of Locamerica. These expectations depend on the performance of the sector, the general performance of the country and conditions in the domestic and international markets, therefore, subject to change.

Today with us, we have Mr. Luis Fernando Porto, Chairman and Mr. Jose Azevedo, CFO and Investor Relations Officer.

Now, I'd like to pass the floor to Mr. Luis Fernando Porto. Sir, you may proceed.

Luis Fernando Memória Porto {BIO 17175861 <GO>}

Good morning. It is with great pleasure that we begin another call for results of Locamerica, the first after becoming the largest car rental company in Brazil. We're very satisfied with the performance obtained by the company in this quarter. Before going on to the main indicators of the company, I'd like to talk briefly about the merger with Auto Ricci, especially concerning the mapping and capture of synergies.

Going directly to slide number 4, we show the four sources of synergy in the merger. They are refinancing the debts of Ricci, renegotiation with automakers, optimization of the organization chart, and elimination of redundancies, and fourth, renegotiation with suppliers and also, the adoption of best practices, especially concerning customer service and maintenance management.

As we can see during Q2, we concluded successfully the refinancing process of 100% of Ricci's debt. And also we took advantage of the good receptivity of the credit market to extend the debts of Locamerica.

In June, we issued BRL 450 million in debentures at a cost of CDI plus 2.1%. In comparison with the previous cost called by Ricci, this should generate savings for the company in the very short term. The speed at which we were able to refinance Ricci's debt right after the conclusion of the merger was possible, thanks to the solid capital structure of Locamerica. And also, Fitch Ratings has given us in June the credit AA-, which made Locamerica the company with the second best rating in the sector. We'd like to show, as you can see, that the merger did not bring any deterioration of our covenants since Ricci had solid credit goals at the time of the merger.

On the right, we see that after the loans in 2017, we reinforced the liquidity of the company and we have BRL 345 million in cash of volume. That is 1.6 times higher than all the commitments we have, all the payments we have in the next six months.

In relation to the purchase of automobiles, we'd like to say that the automakers really appreciated the merger. We had discounts. And now, our discounts for Locamerica will be applied to Ricci, the depreciation of the company and the company (00:05:11) and this will help us in competitiveness.

Now, talking about operational aspects of the merger. During Q2 2017, we hired consultancy companies to help us to define the organization chart and the mapping of possible synergies coming from redundancies in the new organization chart. And thus, we already captured some gains and were implementing them.

These consultancy companies helped us to identify the best practices in rental and also the sale of used cars up to three years of age. We have a great potential for gains with our service and also management of maintenance, points where Ricci was very strong and will definitely bring all these expertise to Locamerica, decreasing our operational costs and increasing the rate of renewal of contracts with our clients.

Before going on to the next slide and talking about operational and financial results during the presentation, we would like to clarify that in order to preserve the comparison of the numbers in Q2 with the previous periods we are working on, we are reporting individual numbers for Ricci and Locamerica.

All the impact that - all the impact is here on this line because since we're recording Ricci's numbers only after May 11, the company's view concerning a complete quarter with both companies together would only be possible in Q3 2017. And in order to have transparency at the end of this presentation, we will give the pro forma numbers of the company concerning the first semester of 2017.

Now, going on to slide number 5, we'd like to talk about the highlights of the quarter. On the upper left corner, we see that once again, we had a positive results in Seminovos cars that are sold. We had a record in profit and gross margin reaching BRL 14 million and 12.1%.

On the graph on the right, we see the evolution of EBITDA of Locamerica. In this quarter, it reached BRL 65.5 million and also a record in margin reaching 64.5% in margin. We'd like to remind you that we're working with recurring numbers. In order to make the numbers comparable we excluded all the consultancy expenses and also financial consultancy, and all the expenses related to the merger. Here, with the graph on the left we show here the net recurring profit going from the reported one of BRL 9.9 million (00:08:24).

Now, we are excluding the non-recurring expenses and also the positive contribution of 40 days of the operation with Ricci. So, the net profit for Q2 2017 in comparison with the previous quarters was BRL 12.6 million. As you can see on the graph on the right, this profit is very in line with Q1 2017, and represents a growth of 66.4% in relation to the profit of Q2 last year.

Even more important than this, we see that for the second semester, we reached our net margin upwards of 12%. Thus, giving us a new standard of profitability. Here, on slide number 7, we see the automobile sector. As we can see on the graph, the sale of new cars had a growth of 9.4%, upper left corner.

In our opinion, this is due to the weak basis of last year. But it still reflects. It's also good news for the second and even more important we'd like to stress, not only the growth of the used car market and especially the strong expansion of Seminovos, which grew 23.3%, as we can see on the graph.

On slide number 9, we some commercial indicators of the company. We see on the upper graphs that both the pipeline of opportunities and mainly new contracts had a significant growth in Q2 2017. During the last three months, we closed 2,352 automobiles in rental contracts. The highest amount since Q3 2015. On the graphs below, we see the evolution of the average fleet age. After beginning their renewal process, we have a drop in relation to Q1 2017 and reached 18.9 months.

Here, we see the average utilization rate, 96.8% in line with the numbers considered as excellent for us. Here, we see the evolution of our fleet, bearing in mind only

Locamerica's fleet, excluding the impact of Ricci, we closed Q2 2017 with 27,408 cars, very similar to the previous quarter. When we've taken to consideration the cars from Ricci, the consolidated fleet reaches 43,000 vehicles. Thus, we become leaders in the rental of fleets.

Here on the right, evolution of cars in inventory. For the first time of the company's history, less than 1,000 vehicles, representing 3.5% of the total fleet cars available for sale. Here, we'd like to stress that this was possible due to a high productivity of our retail stores and excellent speed in the process collecting, preparing, and transporting those cars to be sold. To comment on financial results, I'd like to pass the floor to Mr. Azevedo, our CFO, our new CFO, and I'd like to welcome him on behalf of all of us here in Locamerica.

Jose Antonio de Souza Azevedo {BIO 20187090 <GO>}

Thank you. It's a pleasure to be part of this team at this very interesting time for the company.

Going on to slide 12, we see here net revenue from rental. As we can see in these graphs, both the semester and the quarter were marked with stability in the number of rental days and average tariff. So, the net rental revenue was stable in both periods.

Going on to the next slide, we comment the sale of Seminovos cars that are sold up to three years of age. We see a strong sales with a growth upwards of 30% in the quarterly comparison, and also in the semester, once again, the strong expansion of billing through our retail stores, which went from 44.3% of sales in the first semester of 2016 to 63.3% in Q1 2017.

On the graph on the right, we see that this migration has had a positive result on the profitability of Seminovos, closing Q2 2017 with BRL 14 million gross profit, representing 12.1% in margin. The highest numbers achieved by the company in the company's history.

Here, we see the EBITDA margin on page 14. In this semester, we had a strong increase of costs due to the fleet getting older. As Luis said, we are renewing the fleet and we hope to have a reduction in these costs in the next quarters.

Still on this graph, we see a small expansion of expenses with SG&A. This is the investment in new stores for retail sales. Finally, I'd like to show the excellent contribution of the profit from Seminovos, 12.1% contribution to EBITDA. As a result, EBITDA margins and EBIT recurring, reached 64.1% and 40.4% EBIT, EBITDA was 64.1%. Both of these numbers are records in the company's history.

On slide 15, on the upper left corner, we see the financial expenses. We're excluding the non-recurring expenses concerning the prepayment of some debts and also deferred fees anticipated. As we can see during the semester, the net financial expenses had a drop of 14.1% due to the decrease in leverage of the company and also, better capital allocation of capital. In here, we see in Q1 2017, the finances consumed 27.9%, a drop in relation to the previous year, 6.5%.

In net income, we see the recurring net income, this considering all the extraordinary items and also the partial results due to the merger with Ricci. During Q2 2017, we had a BRL 26 million growth in relation to the same period 2016. On the graph on the right, we see the evolution of ROE, the main metric that we use for return here in management. As we can see, the last five quarters were marked by a positive evolution in the company's ROE, closing Q2 2017 at 16.6% on an annual basis. We understand that this increase in profitability shows the success obtained by the team creating value for the shareholders.

And since we want to be more and more transparent, we have on slide 17 (sic) [slide 16] (00:16:02), Ricci and also Locamerica's numbers, page 16 sorry. Here, we'd like to stress the excellent EBITDA margin of Ricci in Q2 2017 reached 70% higher than the - much higher. We see that the capture of synergies and in depreciation and also in financial results, may take the company to a new level of return. And we'd like to reinforce that we're totally committed in management to do this.

Now, we'd like to begin the Q&A session.

Q&A

Operator

Ladies and gentlemen, we'd like to begin the Q&A session. May we remind you that press professionals may ask questions after we conclude the Q&A session with market analysts. The first question comes from Renato Tano, Safra Bank (00:17:22).

Good morning, Luis Fernando, Jose Azevedo. Congratulations for the results. I have two questions. The first concerning the volume of the fleet that was flat in this quarter. So, what can we expect during the rest of the year?

And the second question, concerning acquisitions, the volume of purchase of vehicles increased and now Locamerica has more buying power, bargaining power. How much more discount do you expect to obtain?

Good morning, Renato (00:18:04). Thank you for the question. First of all, today, as of the beginning of the year, especially in this quarter, we have new era in the company and we're back to growth. All the pillars we've had for the last three years, we've been working on them to make internal improvements and we're now reaping the results with excellent performance, and now, we would like to begin our growth phase.

Now, we hope that in the next quarters, we will increase the number of contracts and the volume of the fleet may be 5% or 10% higher in the next few years. So, this, if we consider organic growth. Now, in terms of automakers, they - we had an excellent receptivity. Initially, we imagined that the discounts of Ricci would be the same as Locamerica, but we see that we may get 1% or 2% better prices, more discounts with the two companies together due to the higher volume.

This is not 100% guaranteed. We're negotiating, because the volume of the two companies is beginning to be seen in the automakers. We believe that another 1% discount or even 2% discount for the total purchases may be possible.

Thank you. Very clear. Thank you.

Thank you. Good morning.

The next question comes from Renato Hallgren, Banco do Brasil.

Q - Renato Hallgren {BIO 17989415 <GO>}

Good morning. Congratulations for the result. My question is in line with the comments on the growth of the company. We have been seeing in Q2 2,300 extra vehicles to be rented. I'd like to understand first if you can tell us from which sector are these new sectors coming from? Where do we see the growth coming from? In which sector do we see the growth or the recovery of the economy?

And I'd like to understand how you see the - what is your expectation concerning the growth of Locamerica? So, will you increase only market share or do you want to get new clients and offer this solution to clients that don't outsource their fleets? Where is the growth coming from?

A - Operator

Good morning, Renato. Thank you for the questions. First of all, the new contracts in this quarter is in line with our sales strategy. It's very pulverized. We did not have any type of concentration in one client or in one sector. It's, as I said, we're getting ready for this for three years to grow and the restructuring of our sales department is also part of this plan.

So, we have a very large sales organization all over Brazil with focus on all the sectors of the economy. We don't have one sector where we don't have an experience we have - or present in all the sectors and we're up (00:22:21) for all the sectors, too. So, first of all, it's very pulverized and in line with our sales strategy.

Now, concerning the recovery of the economy, I wouldn't be able to say that this is a recovery of the economy, no. But we can analyze in the following way. First, our sector in the last two, three years during the crisis has had a good performance. Reminding you, today we have 11% of the vehicles in Brazil that are outsourced by the companies.

And the total number of cars and companies is 5 million. So, we have a lot to explore. So, we don't see it as a recovery, but in some areas, we see a better situation and we credit this to our positioning in sales, our strategy in sales growing with the same responsibility we had in the past.

But today, we are a much more competitive company. In the last three years, we reduced, for example, by 50% our administrative cost per car. We increased the fleet and we

reduced year-after-year, our costs with vehicles. So, in this item, we're much more competitive.

In terms of debt, we have one of the cheapest debts in the market and also a long profile and the second best rating in the market. So, growth will come from a new base, a new structure in sales, and the competitiveness, especially in administration in the purchase and sale and also in the debt, giving us a very strong competitiveness.

Your second question, our growth. The objective, and we have a sales structure focused on this, is to reach new markets by our experience. We know that new clients that come to our model, they are in search of robust companies that have a good history of service to clients and they are willing to pay a little more because it's a new experience and requires care.

So, we intend to maintain or grow our market share. If we have the opportunity with profitability, we will. And our focus is to bring new clients to the base because this generates more profitability for us, and also to look for small and medium-sized clients that are those clients that work with small rental companies, and these companies have better margins and less bargaining power. So, this is the company's growth strategy for the future.

Q - Renato Hallgren {BIO 17989415 <GO>}

Thank you. Excellent. Thank you for the answers.

A - Operator

Thank you, Renato. Good morning.

The next question comes from Álvaro Frasson, Eleven Financial Research.

Q - Álvaro Frasson

Good morning. Congratulations for the results. I'd like to ask about the market share in cars sold. The result was very good in - financially, but the market share is small. What is the target for the medium term and long term?

A - Operator

Good morning, Álvaro. Thank you. Well, as you well observed, this market, Seminovos, used cars that are sold up to three years of age. The largest seller does not have 1% of the total market. So, it's a very pulverized market and we show our position in terms of market share to demonstrate to the market that it's not - if this market decreases - suffers a decrease in its growth rate in the last three, four years, this market has had a lot of growth. We would still have a low market share, demonstrating that it's a very pulverized market.

So, we believe that with the current competitiveness, the products we have, the logistics and the scale we have, we have really an advantage in this market. Enabling us to say that if the market is not so strong in the next quarters, we will be able to conquer even more market share without losing market share or sales. So, we have this - to give you a goal would be difficult. As you can see, our participation is 0.35% of total sales.

So, if we grow a lot, we're talking about 0.5% or 0.6% or if it drops, we can see these numbers. We'd like to say that we have a competitiveness due to the scale of the products and our network of retail stores in our experience that allows us to really be calm and understand that these results are possible in the long term.

Q - Álvaro Frasson

Thank you. Congratulations for the results once again.

A - Operator

Thank you.

The next question comes from the webcast, Mr. Rodrigo Glat, GTA (00:28:52).

With the higher EBITDA margin of Ricci in relation to Locamerica, can we expect a higher EBITDA margin upwards of 70% after you capture the synergies and also with the adjustment in the leverage of the company. How does the company see the pipeline of acquisitions from now on?

Good morning Rodrigo (00:29:23). Thank you for the questions. Well, before the merger with Ricci, we were already looking at higher EBITDA. We're very happy to get to close to 65% EBITDA margin, and you said very well, Ricci is at 70%. So yes, we believe we can in the consolidated company, close to 70% EBITDA, we will try to reach this in the next two or three quarters. Concerning acquisitions, Locamerica, with its solid management base and a capital structure that is robust and this was done in the last few years. In 2016 at the end of the year, we did a strategic plan, aiming at the next five years and obviously, in this strategic plan, we have a plan for acquisitions.

We made a small acquisition, the merger with Ricci and this allows us to say that, today, we have an embedded technology to make small acquisitions, acquisitions that only makes sense with the purchase without exchanging shares or anything, classic purchase or now, with the merger with Ricci, we can also have embedded in the company in the next 90 days, 180 days, an important technology to really go to a new level. So, we want to capture the synergies with Ricci, but as you can see in the last 90 days, we dedicated ourselves to do the business plan. It is ready and it is being implemented.

So, I believe that in another 90 days or 180 days, we may be able to make other business analysis. It's not our main route, I will tell you. We already made three in six months. And maybe, now, we can spend two years maybe without any other. You know that the mortality rate in this kind of business is very high. But we want to say that, yes, we have a strong expertise for this type of business, and our cash allows this and our operation is

doing very well. Yes, we are ready to study specific cases if they appear in the next quarters. So, it may be a route that we may choose.

Thank you. Since there are no more questions, the Q&A session for market analysts is over. Before we go on to the Q&A session with press professionals, I'd like to pass the floor to Mr. Luis for his final comments.

A - Luis Fernando Memória Porto {BIO 17175861 <GO>}

Well, right now, I'd like to thank once again for the presence of all of you in our conference. We understand that in Q2 2017 this was the end of the turnaround phase of the company, where we have focused on our way back to profitability and strengthening of Seminovos retail stores.

From now on, we begin a new era to capture synergies with Ricci. And as we said previously, well, give us an important increase in competitiveness and allow us to grow once again.

Finally, I'd like to reinforce that our Investor Relations team is available to work with you, and we wish you a good day. Thank you.

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