Q1 2015 Earnings Call

Company Participants

- Adolpho Souza Neto, Chief Financial Officer
- Carlos Marinelli, Chief Executive Officer

Presentation

Operator

Good afternoon everyone. Welcome to Grupo Fleury's 2014 First Quarter Conference Call. Mr. Carlos Marinelli, CEO and Mr. Adolpho Souza Neto, CFO and Head of IR will present the results. This event is being recorded and all participants will be in a listen-only mode during the company's presentation. After Grupo Fleury's remarks, there will be a question-and-answer session. At that time further instructions will be given. (Operator Instructions)

This event is also being broadcast live via webcast and may be accessed through Investors Relations website at fleury.com.br/ir, where the presentation is also available. Those following the presentation via the webcast may post their questions in advance on our website. They will be answered during the Q&A session as long as we have enough time.

Before proceeding, let me mention that forward statements are based on the beliefs and assumptions of Grupo Fleury's management and the information currently available to the company. They involve risks and uncertainties because they relate to future events and therefore depend on circumstances that may or may not occur.

Investors and analysts should understand that conditions related to macroeconomic conditions, industry and other factors could also cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Carlos Marinelli, CEO of Grupo Fleury. Sir, you may begin.

Carlos Marinelli

Hello, good morning, everyone, and thanks for your interest and presence at this conference for the first quarter of 2015 results of Groupo Fleury. It's a pleasure to have you with us. For us from the management, the result of this first quarter of 2015 reinforces the evolution of the company and its results, with gross revenues close to BRL500 million and a growth of 13% on net revenues, we demonstrate the potential of our brand operation and market.

The resumption of our accelerated growth, which already been shown on the first quarter 2014, presents consistency in this first quarter 2015 results, with Fleury brand growing 12.5%, hospitals 16.4% and the main highlight, Rio de Janeiro reaching a growth of 14.5%. Now [ph] that have shown on those figures, we reinforce our commitment to the gradual and sustainable recovery of the company profitability to historical levels.

Excluding non-recurring effects, we reached an EBITDA of BRL96.7 million, representing a 21.6% margin in the quarter, an increase of 563 bps of year-over-year. Also in net income excluding non-recurring effects, we delivered a significant expansion of 48.6% reaching BRL41.1 million in the quarter. We continue to improve our management practice with better costs and expenses management through the matrix budgeting, seeking [ph] more synergies in our operations and business and most importantly, we have increasingly bringing more attention to what I have been calling execution discipline, paying attention to daily results, planning and property proactive [ph], managing demand and supply and focusing on welcoming our customers have been key drivers of our managers and employees.

Growth and increased profitability are important measures to bring consistency to our results. For the sustainability of these comes with the trust and loyalty of our customers, the physicians or patients.

Just to remind one of the performance measures closely watched by all of us in Grupo Fleury. Our customer satisfaction index grows 3.1% on a year-over-year basis. Our measure of NPS, net promoter score improved 586 basis points in the same period. As you have all been following the numbers disclosed today are the results of restructuring actions we have been implementing for some time. 2014 was the best year of change and review of our business portfolio. Management in attention to our portfolio of services and payers have impacted that have demonstrated the effectiveness through consistent results.

One example is the acceleration of growth to the double-digit level in the first quarter 2015. We will continue with our premium brand expansion strategy and repositioning of the other regional brands powers [ph] the upper intermediary segment. We believe that this strategy meets a latent market demand for higher quality services in the geographies, where we operate and it also (inaudible) results we desire.

As I mentioned before, Rio de Janeiro recorded a growth of 14.5%. This is a demonstration of the revenue recovery in the region. (inaudible) considering client base after excluding a large operator in the fourth quarter 2013. The robust growth of 12.5% of Fleury brand is a clear sign of the demand for the differentiated product services and of the brand's reputation.

Another highlight is the operation in hospitals, which grew 16.4% after the segment repositioning to provide services in institution that focused on high complex cases. The profitability continues in a gradual recovery based on the continuous efforts on cost controlling despite the high inflation. Last year's actions led to evolution of fixed costs and improvement in productivity [ph]. As a result, cost of services decreased through comparing quarters. We should not forget to mention the fact that operating expenses were strongly impacted by the company's adherence to the Sao Paulo municipality's tax installment program to settle debts related to the Health's Solid Waste Tax.

We paid in April BRL27 million related to the periods between 2013 and 2014. On the subject Health's Solid Waste Tax, it's important to say since 2003, the company have been discussing in a collective action led by SINDHOSP, the Union of Hospitals and Laboratories of the State of Sao Paulo, the constitutionality [ph] of this fee.

In 2011, we had a federal decision on a permanent basis. However, we still feel a termination action and obtained a federal decision, but not permanently in 2013. These actions cannot be get completed, because it's awaiting trial embargoes by the Sao Paulo Court of Justice and that even be taken later to the Federal Supreme Courts. Considering the uncertainties regarding the success of this action and the deadline for the final decision along with extremely favorable conditions of the installment program, which allowed a discount of 75% of fines and 85% on interest rates, the company decided to join the program and pay out these debts.

This generated a non-recurring effect on our cost and impacted our net income on BRL18.3 million. Considering this item, the reported EBITDA margin was 16.3%. Since the payment of this fee was out [ph] in April, the cash impact will be recorded in the results of the second quarter, and those will detailed its impacts throughout the presentation, but I would like to reinforce two points while comparing these quarters.

In 2014, the result of the first quarter was boosted by a reversal of BRL18.4 million in ICMS provisions, are on being part of agreement. Whereas, excluding non-recurring items in both quarters, we had a significant improvement on the main indicators. EBITDA grew 52.7%; operating income increased 88.1%; net income 139% and cash net income 48.6%.

Now I'll pass to Adolpho Souza Neto our CFO and the RI. Adolpho please continue.

Adolpho Souza Neto {BIO 21636124 <GO>}

Thank you, Carlos; and hello, everyone. I will continue this presentation on slide five detailing the growth of our business lines. The 12.1% increase in gross revenue of Grupo Fleury was driven by consistent double-digit growth of Fleury brand. From this quarter on, Fleury will add revenue from check-ups. In parallel, the Rio de Janeiro operations contributed to consolidated growth with a 14.5% increase. This quarter the comparison base already excludes the impact of the main structural actions of repositioning implemented in the region during the fourth quarter of 2013.

Among Rio de Janeiro's highlights, it's worth mentioning the significant revenue growth is internal, a clear result of inclusion of the service in the mix offered by Felippe Mattoso and Labs [ph] brands.

On slide six, the revenue per square meter shows an increase of 9.1% between quarters as a result of the maturation of opened and ex penetrations [ph] of expenses in early

2014, including the (inaudible) and Rochavera PSCs of the Fleury brand and efficiency gains in existing PSCs.

Gross revenue per PSC grew 14.7%, while the average price increased 7% between quarters. In the last graph, we see the same-store sales following the growth trends increased in the third quarter of last year, reinforcing the focus on asset efficiency and the offer of a more diversified and complex portfolio mix.

Slide seven shows the recovery of Rio de Janeiro's share in Group Fleury's revenues as well as the growth of the Fleury brand that represent 60.8% of PSC revenues.

Slide 8 shows the PSC's growth by business. Indicator of gross revenue per square meter of regional brands was impacted by an expansion of the a+ brand in PSC in the first half of 2014. The consolidated average revenue per brand is 7% the combined effect of portfolio improvement, repositioning of regional brands and price renegotiations.

On the next slide, we highlight that operations in hospitals grew 16.4% driven by the strategic repositioning to focus on highly complex institutions. Same hospital sales operations also stand out with a 9.1% growth.

The next slide number 10 shows the reduction of allowances and deductions by 78 basis points. Deductions represented 3.4% of the gross revenue in the third quarter against 4.2 in the first quarter of 2014 -- in the quarter against 4.2 in the first quarter of 2014. Net income in this term [ph] grows 13% to 447 million in the period.

On slides 11 and 12, we see some indicators of the cost of services. On slide 11, we see that the overall trading cost was significantly lower than revenue growth, an increase of 5.6% compared to 12.1% of the gross revenue growth. The number of employees remained stable at about 9,000. The service area in PSC increased by 2.5%, while the number of units of PSCs decreased by the same level. The opening of new units was focused mainly on the Fleury brand with the opening of the (inaudible) PSC and expansions of the Braz Leme and Rochavera PSC. In addition to that there were specific adjustments units in our other brand.

On slide 12 this highlights good management of general services and while general expenses, which decreased 12.6% in the period and the line of general services and rents that had an increase in loan equation.

On slide 13 there is a breakdown of these costs, which totaled 322 million in the quarter and presented 72.1% of net revenue, the decrease of 5 percentage points versus 2014. The highlight here was the line of personnel and medical services, which recorded a decrease of 161 basis points, representing this quarter 36.3% of net revenues, impacted by better management of medical costs, which has been low or bearable.

On slide 14, there are details of operating expenses, which were impacted by 24.1 million for the Health's Solid Waste Tax and 4.2 million in the quarter for the fixed assets writeoffs related to an inventory account. Excluding the non-recurring items, the analysis indicate a 93 basis points reduction as a percentage of net revenues.

On the next slide, we see the EBITDA bridge, while reported EBITDA were stable at 72.7 million, excluding the effect of non-recurring items in the two quarters analyzed, we see a significant improvement in March, which increases from 16% to 21.6% due to the effect of the management of costs and expenses and the operating leverage coming from the robust revenue growth.

Turning now to the below the line, we start on slide 16, showing the profile of our debt, which is composed mostly by deletions of the debentures of 2011 and 2013 with maturities expanding up to 2020. (inaudible) that represent 10% of our finance and has a very competitive interest rate. The cash balance at the end of the first quarter was 471 million and the Group ended the quarter with a net debt of 579 million, which represents a 1.9 times ratio to EBITDA.

Moving to the next slide, we see that the financial results for the quarter, where a net expense of 18.7 million compared with an expense of 3.8 million in the first quarter of 2014. But with both periods being strongly affected by the effects (inaudible) of non-recurring items. Without this effect the expense in the quarter (inaudible) increase reached higher net debt level and increase in the Selic rate that would be lowered by 20 basis points as a percentage of net revenue.

On the next slide, number 18, we see that our rate of income tax and social contribution in the quarter was 44.6% higher than the same period last year mainly due to the fact that part of the non-recurring expenses recognized in the quarter are non-deductible. Another important point to note is the fact that most of the tax was deferred in the fiscal use of the goodwill on acquisitions, where at the end for a very low cash tax, which represented a rate of only 6% of EBT, earnings before tax.

On the next slide, we see on the right side the value of the use of the goodwill for this year and the next two years as well as the reconciliation of EBITDA and net income, which was 13.4 million for the quarter down from 2014, but if we excluded the effect of the non-recurring items in both quarters would represent an increase of 139% from 13 million in 2014 to 32 million in 2015.

The next slide is number 20 [ph], shows the profile of our accounts receivable at the end of the quarter, where we see the maintenance of the level of the past due accounts of 120 days, as a percentage of total receivables by 18%, and the increase of the provision coverage index. At the same time, we see a slight variation in the Group's aging that send accounts receivables (inaudible) 120 days. But we see this as a temporary effect that should be normalized as we finish negotiations with SINDHOSP plan operators.

Moving to slide 21 [ph] cash generation, we see that our operating cash flow in the quarter was 6.3 million compared to a generation of 29.7 million in the same period last year. The decrease in cash flow was mainly due to the decrease in cash flow was mainly due to the higher consumption of working capital, mainly accounts receivables due to the increase in gross revenues and an increase within one of our customers on the hospital business with whom we practiced the shorter payment term with lesser [ph] discount that was higher than our cost of funding. We eliminated this discount and returned to the regular payment terms with this customer, which caused a permanent impact in our average collection periods, but from an economic point of view is best for the company.

Investments in CapEx which are detailed on the next slide, stood at 17 million in the quarter, concentrated in IT spending, because we are doing reimplementation of the SAP system and we have completed integration of the front office system, while imaging that in the Rio de Janeiro region; another initiative that will improve service to our customers and create efficiency. For the rest of the year, we should see a return to the budget distribution of the CapEx spending. We see investments in expansion represented in majority of this local spending.

The last two slides show Fleury's share performance in the quarter and the investor related agenda for the coming months. We have already scheduled conferences and NDRs for the month of May and August, our events that are stated on the IR website as well.

We'll now turn to the Q&A session.

Questions And Answers

Operator

Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions) This concludes today's question-and-answer session. I would like to invite Mr. Carlos Marinelli to proceed with your closing statements. Please go ahead Mr. Carlos.

A - Carlos Marinelli

Just to thank you all again for being with us in this conference for this first quarter of 2015. And we will be more and glad to have you on other opportunities here at Fleury or other investor's conference to answering you, your questions or -- on our company. So, thank you again and have a good day.

Operator

That does concludes the Group Fleury audio conference for today. Thank you very much for your participation. Have a good day and thank you for using Chorus Call.