

Q2 2020 Earnings Call

Company Participants

- Gustavo Sousa, Chief Financial Officer
- Paulo Caffarelli, Chief Executive Officer

Other Participants

- Jeff Cantwell, Analyst
- Jorge Kuri, Analyst
- Neha Agarwala, Analyst
- Tito Labarta, Analyst

Presentation

Operator

Good afternoon, everyone, and thank you for waiting. Welcome to Cielo Second Quarter of 2020 Results Conference Call. With us here today, we have Mr. Paulo Caffarelli, Gustavo Sousa and Jean Leroy. This event is being recorded, and all participants will be in a listen-only mode during the Company's presentation.

After Cielo 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 Cielo's website at ri.cielo.com.br/en/, where the presentation is also available.

Participants may view the slides in any order they wish. The replay will be available shortly after the event is concluded.

Those following the presentation via the webcast may post their questions on our website. They will be answered by the IR team after the conference is finished.

Before proceeding, let me mention that further statements are based on the beliefs and assumptions of Cielo management and on 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'll turn the conference over to Mr. Paulo Caffarelli. Mr. Paulo, you may begin your presentation.

Paulo Caffarelli

Okay. Thank you to all of you for taking part in this conference. Good morning, everyone. Good afternoon for us in the Group. The results of Cielo, the leader of the payments industry in Brazil in the second quarter of 2020. To stress the impact of the most devastating health global crisis in 100 years. Cielo accounts for approximately 40% of the Brazilian payment industry, and we have had a heavy shortfall after COVID-19 outbreak. Some aspects are worth mentioning, the Brazilian governance guidelines prohibited more than half a million to operate temporarily or permanently persisting the biggest situation drop according to IPCA and ICVA from our Cielo's index. The constraints, they're from basic to luxury-goods which projection is around 40% this year. Cateno's operation has faced with the same impact considering the lack of reduction after the consumption which credit and debit card from Banco do Brasil customers. And finally, the real currency devaluation also affected the consolidation of the results of our foreign participation, which we will talk about nationally in United States. No doubt that the second quarter of 2020, was a unique little moment not only in terms of challenges but also opportunities.

Cielo has been challenged to go beyond the POS and to reinforce its (inaudible) as a platform Company, we may do things under the governmental guidelines. It has been possible due to our restructuring to face the transformation to become a tech company. We had -- we mentioned the company and adjusted bills payments to face the new markets. We adjusted costs, launched

New products reset the business model and we reduced the leverage to all-time low level in the ongoing management.

Cielo has been evolved in key solution such as what is a payment system operator and also as the Whitelabel platform that guarantee selling solutions for our customers such as Ambev. Cielo keeps challenging itself. Having said that, we are optimistic in regards to the second half performance of 2020, however, it's worth highlighting that the losses of the first half mainly the second quarter that was entirely negative, we want to be offset. We are dedicating our efforts to lay the foundations for the coming years.

The market is really building itself in order to fit customers and users in new digital demand in terms of payment system. Considering that Cielo is the leader of the segment, we will keep heading the ways in digital solution reinforcing our regular business strategy based on raising the participation of the retail segment and increasing the penetration of credit products. As a result of this, even in the midst of the crisis, with the tail-end months of the new segment accounts for 36% of second quarter to -- volume, 31.4% over the first half of 2019. Moreover, Cielo achieved 29.6%, all-time high of pre-payment (inaudible) another positive experience related to our sales force, which even working remotely with multi, was able to over-perform and bringing new clients into Cielo's base, making it bigger than before. This is one of the signs of the new normal in Brazil even abroad the (inaudible) agency and agility since have provided connection between buyers and sellers into one single platform, facilitating the delivery of logistics in

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compliance the social distance safety guidelines. In addition, NFC and QR Code tech solutions were triggered to 80% from 40% last year (inaudible).

Furthermore, we have range of (inaudible) probably the payment solutions offering broadly Super Link, which is a product developed two years ago, during the pandemic period, Super Link became the perfect solution to the new (inaudible) reality explaining our customer base in 100%. Year-to-date (inaudible) Southern and 1000 versions ready to move and in and in about the volatility the consistent the (inaudible) selected (inaudible) acquired exported should provide a fire in to payment solutions into only dwell on sensible to us.

Its production is under evaluation by the Brazilian Financial regulator Banco Central and we do hope that soon we are going up in the Brazilian markets -- in the Brazilian market. The digital transformation is the reality, and (inaudible) is the channel. Connecting both Cielo's innovative and safety payment solution creates a key role in the recovery of the Brazilian retail economy. And finally, leading the way Cielo's participation goes even bigger to support the Brazilian government to deploy the emergency financial absolutely, reaching up to 6 million people who might do not have bank account. Cielo is extremely committed to the new reality, although it's a very sad moment concerning to -- concerning the health of the population, we've seen this crisis also as an opportunity to remain strong, be more efficient, strengthen bonds with our customers and above all, maintaining our leading position. reflected (inaudible) to just to reinforce to it, that it's important to see these kind of low comparable variables related to the COVID-19 crisis, mainly drop in volume in Brazil in retail, another few of this relating to our Company. Cateno has suffered the same situation like us, in terms of reduction of production and the (inaudible) related to the exchanged evaluation, because when we analyzed our operation abroad, in the United States, initially (inaudible) We didn't have the same forecast that you had acquired for -- this case, the second quarter fully committed into the guidance.

We hope that the next second -- third quarter and fourth quarter will going to be much more volume for us in terms of retail and in terms of corporate as well. I hope that we can have our (inaudible) as part of this, but we believe that the most part that we had lost in the second quarter, we want to be -- we want to recover in the next quarters.

Thank you so much, I'll pass to Gustavo.

Gustavo Sousa {BIO 17683157 <GO>}

Thank you, Caffarelli. And Hello everyone. I'm going -- because we had people following us via phone call and also via the webcast, I'm going to be referring to the number of the slide, so that phone call participants can follow. And so that webcast operator can also change the slide. So, I'm starting the presentation on page 2 on page 3 of the material. And let's start with the boxes on the left. What we have is a comparison of the month of April, May and June with comparable base of February. We do a comparison of before and after the crisis and the effects in those months. With that nominal broad retail sales, the ICVA index prepared by Cielo, which is a reflection of the Brazilian retail activity, we had a decrease of 30.3% Cielo's TPV on the same comparison decreased by 26.5% and Cateno's TPV decreased by 24.8%. In the same period during this crisis, we saw increased

productivity in the commercial and in the administrative teams we'll see slide talking about that in a few minutes.

We also saw a strong increase in the penetration of term products in SMB, and in the long tail we reached almost 30% of penetration, and we also saw increased usage of digital solution, and we also talked about -- talk about that in more detail in the upcoming slides.

Now going to Slide 4 of the presentation. On this slide, we see the month-to-month impact of the crisis on the three metrics that we saw on the previous slides. On the ICVA, we had a 37% contraction in April. This contraction improved to 22.4% contraction in June, and in July, we are showing the first 22 days of July, we had a 15.7% contraction on ICVA. So not only on ICVA but in all of the metrics, we are seeing a gradual recovery.

On Cielo's TPV, in April, we had a 35% contraction, this contraction was at 17.6% in June, and in the first 22 days of July, it's at 8.7% contraction.

In -- on Cateno, in terms of volumes, we've had a 32% decrease in April. This decrease was at 18.4% in June and in the first 22 days of July, we have seen a 14% contraction.

Moving to Slide 5, where we share another metric for following up the impact of the crisis. We see that in March, we reached the bottom of this metric. The metric depicts the number of merchants that with at least one transaction with our equipment.

And with that, you could see that in March in the -- in this information, we had 50% of merchants regularly operating. This metric improved gradually so that at the end of June, we were at 87% and on July 22, we were at 91%. We also see a gradual recovery on this metric.

On Page 6, we use another approach to quantify the impact of this crisis in Cielo and Cateno's volumes. So the methodology we use here was to look at the year-over-year growth of the first two months of 2020 and apply this growth metric to the second quarter.

So by doing this calculation, we arrive at a projected number of Cielo's TPV of BRL178 billion. However, because of the impact of the prices we saw, a number of BRL127.9 billion. Applying the same rationale at Cateno, we see a projected volume of BRL75 billion, but in actual volume of BRL55.5 billion. So by using this methodology, we arrive at the estimated impact of volume decrease at Cielo at BRL51 billion and at Cateno at BRL19.5 billion. By acquiring the revenue yield of these two companies to this volume decrease, we arrive at impact in revenues for Cielo of BRL404 million and at Cateno an impact in revenues of BRL175 million.

Moving to Page 7 with the combination of these effects of Cateno and Cielo, we had lower net operating revenues totaling BRL2.4 billion, in that a 12.5% decrease year-over-year and EBITDA of BRL236 million, and that's nearly 70% decrease and a net loss of BRL75 million in the second quarter.

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Moving to Page 8 and looking at our traditional slide about volumes. We show that on the yearly comparison of the fourth quarter of 2019 to the fourth quarter of 2018, we were showing good growth metrics, specifically in financial volume and TPV, we had a 12.6% growth. However, TPV was really impacted by the crisis that we saw on the previous slide, so that represented a TPV of BRL128 billion in the second quarter. When you look at the client base, a similar dynamic. We were presenting [ph] nearly 18% growth on the fourth quarter, this metrics was also impacted by the COVID crisis. And when we look at the term products we're talking here about the second half by about the (inaudible) and also the about prepayment of receivables. We were showing a growth of north of 18% in the fourth quarter. And now, we saw a decline, this decline is driven by two factors. First, of course, we have the crisis, which impacted volume, but we also have the impact of our strategy of prioritizing capital allocation to SMB and long tail in terms of term products and we do see our capital allocation to the large accounts.

Moving to Page 9, we see an evolution of revenue yield. On the yearly comparison, we had a 3 bps decrease and on the quarterly comparison, we have a relative stability 1 bp increase. This is a change, and we see that on the graph on the right, this is a change to the trend that we had seen throughout 2019, and reflect not only the fact that the other portfolio was already repriced, but also the fact that with lower volume, the portion of revenues, that is fixed for example, our rent benefits this metric.

And now moving to Slide 10, which shows some of the topics that we will talk about in the remaining Slides. Production, Penetration in SMB, and Long Tail, Operational Efficiency, Innovation and Liquidity and Leverage.

So moving on to Slide 11. The metric we present here is the first stage of the commercial efforts. It's the first stage of success, that the hunter gets by presenting a proposal to a client, with metrics we represent that the proposal was accepted by the clients. This doesn't mean that the client has signed the contract or that the client has already received the equipment and he's already doing transactions with Cielo.

We decided to share this early stage with you just to show you how the metrics in June are picking up. So what we show you here is a comparison by using January of 2020 as the base on 100 parameter, and we show you that we did suffer during the crisis in March and April, but as beginning in May, we've recovered this metric to levels that are above the beginning of the crisis, the period that is previous to the crisis.

Moving to Page 12, on the chart in our left, we see the gradual gain of participation inside of Cielo's TPV of the SMBs in long term segment, they represented 31% of our TPV in the first quarter of the last year and they now represent close to 36%. And on the chart in our right, we see the strong increase in penetration of prepaid receivable and (inaudible) happy on the I'm sorry SMBs and long-tail segments. We are now at a record high in terms of penetration in these two segments, fulfilling a strategy and a challenge that we have shared with new analysts and investors in the previous call.

On page 13, we show you some of the assets that we are doing on the cost side. What we show you here on the chart in our left is adjustments on expenses by excluding the

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loan fees completely related to volume, the subsidies on the equipment that are sold and also the fees that we pay to the bank that worked with us in the origination of (inaudible) in addition to also excluding non-recurring expenses. With those exclusions, we show you that in comparison to the fourth quarter, the first quarter presented 15% improvement and we are maintaining the same level of expenses by this comparison. And this is happening because of cost control measures that had to do with changes in the call center operation model, changes in our logistical model, changes in our benefits package and also other restricted measures that may not impact the bottom line greatly, but they are sent to assess method in the culture of cost control, I'm referring to the restrictive measures in travel, in cars for the sales force and also in admin (inaudible).

By this now moving to page 14 of the presentation when we talk about physical transformation and then the number of features there now being improvingly used by our client base such as NFC and our Super Link, our partnership with the logistics company helping our clients and also the usage of QR Code. The volume of TPV done by these transactions by default solution is growing by more than 152% when we compare June to February.

On page 15 we see that a comparison in June throughout the years of new products, they are launched by Cielo and with that, we state that Cielo has the most complete product suite offered to clients.

Moving to Page 16. We have launched the WhatsApp payment possibility which is payments via WhatsApp through the Facebook Pay tool that is processed by Cielo. We work with P2P and P2M, it's as easy as sending a picture to someone and it is now suspended [ph] being evaluated by the Brazilian regulators.

We move to Page 17, when -- where we show you here that Cielo has recently created an area, a new structure dedicated to credit products. This will analyze the needs of our clients and launching new products in the future, but we also share with you products that are already available such as credit backed by receivables, anticipation of receivables, working with some parties and also real estate backed credit.

And on Page 18 of the presentation, we share with you a recent regulatory approval that Cielo obtained the license to be an Eletronic Currency Issuer which will in the short term enable Cielo to have its own payment account, prepaid card, banking services such as money wire in issuing billing documents and also to work with the PIX, the instant payments solution being prepared by Brazil Central Bank. In the medium term, we will also be able to work with many open banking features whitelabel platforms and enhance our data intelligence and reconciliation services.

On Page 19, we show the growth of digital solutions on the chart in our left. We see that year-over-year growth of e-commerce specifically in June, year-over-year we saw a 129% increase. And on the chart in our right, we see here how these transactions e-commerce, NFC and QR code are gaining participation and gaining share inside of Cielo's TPV.

And now on Slide 20, we show you Cielo's liquidity and leverage metrics. Cielo's cash position at the end of the quarter was above BRL7 billion. Cielo's resources invested on the prepayment of receivables were at BRL4.8 billion. Our amortization schedule and other financial obligations is depicted below on our left, you see that most of the short-term will be taken care of in the third quarter and we will have BRL9 billion of debt and maturing in the long term. And we also show you a much-improved leverage metric at 1.21 times by the end of this quarter.

With that, I finalize the presentation and open for the Q&A session. Thank you very much.

Questions And Answers

Operator

Thank you. (Operator Instructions). Our first question comes from Jorge Kuri, Morgan Stanley.

Q - Jorge Kuri {BIO 3937764 <GO>}

Hi, good afternoon, everyone. Jorge Kuri from Morgan Stanley. Two questions, if I may. The first one is on your market share, your TPV was down 20% quarter-on-quarter, we saw GetNet report this morning, down 11% quarter-over-quarter, much better than you did, can you talk about market share losses. Where are you seeing those losses was taking share. What are you doing to reduce that and at what point do you think that will normalize or may be the part that I'm not understanding is the difference, it may be driven by less digital transactions. Is that an issue for you? Are you not being able to capitalize on this surge in digital transactions that we've seen. That's my first question.

And my second question is on, on your JV with Whatsapp. I'm trying to understand the pricing of debit at 3.99%, which for P2M seems very uncompetitive, because everyone else charges 1.99%. And so, why would anyone pay 3.99% for something that's available at 1.99%, and overall on the credit side -- on the credit card side, sorry, no ability to do parcelados which is a huge part of the way Brazilians consume and so it does seem that the structure on the P2M side looks uncompetitive from that vantage point. And so, is that because you're not that interested in the P2M and this is mostly a P2P platform or how do you think that you're going to be able to compensate for that in those shortcomings? Thank you.

A - Gustavo Sousa {BIO 17683157 <GO>}

Kuri, Gustavo here. Thank you for your question. I'll start with your first question and then I'll pass it Caffarelli to talk about the second. On the first question on market share for -- and I'm going to talk very subjectively here because we just saw our competitors numbers in a -- we are still awaiting for second quarter numbers on most of the industry. Right. But what we believe is the trend in terms of market share is that Cielo overall will have a reduction this quarter, mainly because of two factors;

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First, we are doing a work to recover profitability with large accounts and in some clients, we are able to reprice them in a way better terms and with others they lead to the competition. I suspect that the competitors that you mentioned is gaining traction in those accounts, but no, they have their own pricing policy. Another segment where we are likely losing share is on the long tail, we had expected the market that we are way more restrictive in 2020 in terms of (Technical Difficulty). We presented information in our release, showing that in this second quarter, as a result of that, of the lowest subsidies, we sold 42,000 equipments. In this contrast equipment sold in the fourth quarter of last year of 250,000, so we will likely because of the lower, income -- lower inflow of new clients that's driving Cielo's equipment sold. We are likely going to have market share losses on the long-term as well. In the middle of the period that's where we want to retain our (Technical Difficulty) expand because the competition hasn't fully disclosed number yet, I don't know where's the trend will be. What I can tell you is that we don't see market share losses at Cielo as a result of not participating in digital payments and so on, quite the contrary, we launched and enhanced a number of alternatives to our clients in terms of digital innovation. And we see increased usage on that.

To talk about Caffarelli, I would now pass the word to Paulo Caffarelli, Caffarelli please.

A - Paulo Caffarelli

Okay. Jorge, thank you for your question. First of all we need to take in consideration that this currently movement is the first step from Whatsapp in Brazil. In this case, let me talk about LDR for P2M we are talking about it to remove in (inaudible) in Brazil. When you talk about (inaudible) in Brazil, I need to be go through if you 3.99%. It's a very competitive price. If you analyze other acquirers in Brazil. They are pricing sometimes pricing slightly 5%, 6% 80%. In this scheme, there is some kind of (inaudible) financial depletion for the companies, because sometimes, the people, the payments are not interested in terms of interest rate, but they are interested how quickly they can receive their money. Okay? In this case, I think that 3.99% [ph] is very competitive price. We can be very competitive among all the acquirers in Brazil that are in P2M in this segment, in the long tail segment and we believe that for the other places, what can reduce this price when you talk about now (inaudible) or within (inaudible) Because we need to take into consideration in this situation the scalability that we can have in Brazil related to the LDR. At the end of the day, we need to consider as well that P2P, there is no charge in terms of transactions.

Q - Jorge Kuri {BIO 3937764 <GO>}

All right, thanks, Paulo for legal explanation.

A - Paulo Caffarelli

Thank you, Jorge.

Q - Jorge Kuri {BIO 3937764 <GO>}

Just one clarification. I'm looking at the website of PAGS and Stone [ph] and Mercado Pago and (inaudible) and their debit is BRL199 [ph]. So that was my question. So the going rate for debit for micro merchants is BRL199 and you're charging BRL399 so that was my question. How do you see that as competitive? Yeah.

A - Paulo Caffarelli

Yeah. In this segment, this company that you have mentioned, there is no participation because we are talking about in most segments. There are other companies working on this and I can send to you by perhaps (inaudible) the prices among these segments and I can show you that we have much higher prices than we are charging nowadays 3.99%. Are you (inaudible).

Q - Jorge Kuri {BIO 3937764 <GO>}

Thank you. Appreciate it. Thanks a lot.

A - Gustavo Sousa {BIO 17683157 <GO>}

Thank you. Bye-bye.

Operator

Our next question comes from Neha Agarwala, HSBC.

Q - Neha Agarwala {BIO 17722501 <GO>}

Thank you so much for taking my questions. I have three questions, first on the expense side, if you could elaborate a little bit. Even considering the normalized expansion, the total costs this quarter was flat quarter-on-quarter, while the revenue declined with lower TPV. So we thought that some of the cost would be variable, so with a lower TPV those costs would be going down, so why didn't we see the decline in costs and how should we think about cost in the coming quarters? Should they grow, now that the TPV would come to more normalized levels in the coming months, should cost continue to grow here on in the coming quarters?

Then, my second question is on the net adds. We understand that you lost a lot of clients because we reduced subsidies especially in the long-term market. So is that impact, largely done by now? Or should the active merchant continue to decline in the coming months. So, any color on the, the active merchants for this year would be helpful.

And then lastly is on the credit product. I understand that you are working with partners to provide different types of credit options to your customers, but could you give us some color on what is the size of your loan book, what is the profitability of this product for you? And what is the growth outlook that you have? You previously mentioned that you would need to diversify your revenues and go beyond just acquiring. So how much do activities beyond acquiring contribute to your total revenues at this point and how do you see that growing with additions of credit products and other other forms of businesses. Those are my questions. Thank you so much.

A - Gustavo Sousa {BIO 17683157 <GO>}

Thank you, Neha. I do my best to answer your and then (inaudible) have three ways right. So starting with the cost side. So (inaudible) that we presented to you in this material, and also in our release develop attempt to try to make the number clearer to the marketing

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and organic low growth to that. What we are calling in the presentation in (inaudible) would believe as normalize expenses is the combination of cost in expenses with the exclusion of brand fees. The cost item we have -- is related to the most to volume. So the reason you exclude that, you have the variable cost out of the way just to show you that the core of cost is actually, we do. So, because of about this exceeded business, the cost that we would like to see increasing related to volume, right. But, for this normalize extensive calculation that we do, we exclude the brand fees. We also exclude the subsidies of equipment that is sold specifically, because as I mentioned to Jorge on the previous question, the near-term reduce the level of subsidies that we are now great declines on, so equipment in 2020. So that, now throughout the year, we are delivering with the amortization of subsidies that were granted last year, but in 2021 that will not be the case. Specifically because we ask them to buy way less. We also exclude, the fee that we pay to banks that work with (inaudible) origination and maintenance of clients, because last year those roles across, work reduction of revenue and on this year, they are on the cost side. And we also excluded one-offs and extraordinary items, non-recurring items that we presented.

With that, the normalized expenses, show a year-over-year decrease of 5.4% in relative stability quarter-over-quarter. That's a growth of 24%. So, what we are likely to see, Neha, is the continuation of this improvement on the cost side. When we do [ph]point adjustments and the costs, that -- likely grow with the recovery of the briefing economy is the branching, so it's sort of a mixed answer -- of the cost side, you keep going down as we keep it is manage efficiency measures, but brand fees will go up.

Your second question was related to net adds, and specifically in this metric on the client base metric. And we have two effects. One is related to again lower subsidy levels, that we are granting to clients. As I expressed in the second quarter, we saw 42,000 POSs versus 260,000 in the fourth quarter of last year. So this lower entrants of new clients inside Cielo is part of the reason we saw a decrease in client base. The second reason for the decrease in client base has to do with the crisis. We actually had the metrics that we presented for client base is the number of clients that performed at least one transaction with Cielo over the last 90-days. And we saw an increase in this metric. We call this involuntary churn, clients that haven't canceled the contract with Cielo however have not performed transactions with Cielo. So we saw an increase in that completely related to the crisis. What we're likely to see here is a recovery on this metric of clients that did not operate with Cielo.

And we already starting to see that in the early July numbers, we have seen an uptick in client base inside of Cielo, but on equipments that we sold, we are likely to keep seeing a decrease of the interest of clients that buy equipment inside of Cielo. And on your last question talking about credit, the initiatives that we are presenting here are more related to the future (Technical Difficulty) So it's very marginal it's not very significant in terms of Cielo's numbers. We do have alternatives working with partnerships that we presented here in our call that the reason we created the specific area, this new structure inside of Cielo is to enhance this number, because this is still being worked on, I do not add revenue projections or a specific goal to share with you, but we do have high hopes for this new structure that was recently created.

With that, I hope I have answered your two questions.

Q - Neha Agarwala {BIO 17722501 <GO>}

Yes. That's very helpful. On the revenue side, could you please elaborate and tell us, how do you see the revenue growth evolving in the coming years. There, the pressure on MDRs continue and same is with the POS revenues, prepayment had sharply declined this quarter, but I believe that two-day payment optionality is working well for you. So what do you think will be the revenue drivers in the medium-term for the business?

A - Gustavo Sousa {BIO 17683157 <GO>}

We are following the items you mentioned, Neha, we believe MDR is on a continued declining trend, this decline has started this year, but in the long-run we think the trend will persist. The POS rental is also following the same trend. On prepayments, I believe what I can to see growth in overall clients that needs this solution. So specifically one metric that we're very happy to share with you was the increase of penetration of prepayment product in SMBs and in the long-tail. So we're likely to see that growth. So out of the three traditional components of our acquiring revenues, three of them will persist under pressure in our view, and one of them will likely see an increase in product. With that acquirers and business, the reason that we are -- we created this new team, this new area dedicated to new products. We have to diversify their sources of revenue via credit, digital wallets other sources of payments and so on. So that in our view is the trend.

Q - Neha Agarwala {BIO 17722501 <GO>}

Okay. Thank you so much for that. Last thing if I can ask, you're focusing on the middle market, do you have the NPS numbers that you could maybe share with us?

A - Gustavo Sousa {BIO 17683157 <GO>}

We do not have updated numbers, Neha, the last numbers that we talked about was from late last year, we talked about it on the last call, just to give color to everyone on that. We presented a strong growth in NPS when we compare to -- at the end of 2020 to the beginning of 2019 and with that we are at par with what the market call, the incumbent right with our top direct competitors that are controlled by banks. However, we still have a gap to surpass, a gap to work on to reach the levels of the new entrants.

Q - Neha Agarwala {BIO 17722501 <GO>}

Thank you so much, Gustavo.

A - Gustavo Sousa {BIO 17683157 <GO>}

Thank you.

Operator

Our next question comes from Tito Labarta, Goldman Sachs.

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Q - Tito Labarta {BIO 20837559 <GO>}

Hi. Good afternoon, everyone, and thank you for the call. My question is on the prepayments just to look at that a little bit further when you look at prepayment volumes, there were 7.7% of total volumes, I know that's offset by the Receba Rapido which increased a lot. But even if we combine the two both the prepayment and the Receba Rapido. It was around 15% of total volumes. If we look last quarter and last year it was closer to 20%, 21% of total volume.

So if you can maybe -- why did it fall so much? I mean, I think if you go -- grow more in SMBs, I would expect they would demand more prepayment than Receba Rapido. So just to understand, is it just something particularly to the quarter given the impact of COVID-19? Or is this sort of a new trend that we should expect where the total volume should be around the mid-teen? And then in terms of the mix between the two, should we continue to see prepayment fall even further and continue to be offset by Receba Rapido or how -- what percentage of total volumes should come from each, if you can give some more color on that would be helpful. Thank you.

A - Gustavo Sousa {BIO 17683157 <GO>}

Tito, thank you for your question. What we have there is actually a mixed trend. So overall, in terms of the prepayment volumes for Cielo as a whole, we are likely to keep seeing a decrease there, because the big volume driver for prepayments is larger accounts, that's a big volume driver, but that's not the big profitability driver.

What we had been talking about in the last quarter, is that our capital allocation, we moved capital from prepayments in large accounts to the allocation of capital prepayments in SMBs and long tails. So when you look at Cielo overall, you keep seeing as a reduction in that metric.

In addition to this capital allocation strategy, we also had restrictions that were imposed in some clients, namely the big ones, that were more severely affected by the COVID crisis and that are riskier in terms of the impact of the crisis, such as sub-acquirers and clients of tourism and entertainment segments. We restricted the prepayment of receivables in those segments. But that being said, we are shifting capital allocation towards SMBs and the long tail. And in that segment and we do share the information with you in Receba Rapido, we see an increase in penetration. So we are likely to keep seeing this increase persist in the coming quarter. However, because we're talking about increased penetration, but these lower volumes in large accounts, overall, we are likely to see a reduction on the metric for Cielo as a whole.

Q - Tito Labarta {BIO 20837559 <GO>}

Okay. That's helpful. So I guess, maybe to pick up a little bit from this quarter given some of those restrictions. But then, after that should decline over time. And then, what do you see the impact could be from the receivables market and when they get launched? Do you expect significant pressure on pricing from that? How do you think that could impact?

A - Gustavo Sousa {BIO 17683157 <GO>}

We do expect more competitive pricing, definitely. But we still have to see what the market would look like after the implementation Tito. But yes, we believe that the receivables central with uplift (inaudible) will bring additional pricing pressure on receivables.

Q - Tito Labarta {BIO 20837559 <GO>}

Okay. Thank you.

Operator

Our next question comes from Jeff Cantwell, Guggenheim.

Q - Jeff Cantwell {BIO 18876343 <GO>}

Hi, thank you for taking my question. And I appreciate all the details you have given us in your slide presentation and on this call. I wanted to ask you a question about your profitability. So we can understand it's a very difficult time period and then you have to manage through this period, which means maintaining a lot of the cost you've talked about over the past couple of years with the hunters et cetera. And that's clearly impacting your profitability right now.

But, going forward, can you talk to us about your commitment to getting Cielo back to profitability over the next six-months to nine-months, maybe tell us, do you think investors will see Cielo return to profitability in the back half of this year or is that more likely to happen in 2021? Can you just give us a little bit of color on your base case from a profitability standpoint as we try to think out over the next couple of quarters? Thank you very much.

A - Gustavo Sousa {BIO 17683157 <GO>}

Hi, Jeff, Gustavo here. I'll do my best to answer you question and not giving specific projections, because I cannot do that for regulatory reasons, but I'll do my best to answer your questions. So the first comment I have for that Jeff is the fact that a loss at Cielo is something that is not structural. Cielo's earnings profile is structurally positive.

So with that -- what we have seen is completely related to crisis. So the recovery of that also has to do with the recovery of volume. So what we have been seeing and we showed that on ICVA, which shows that on Cielo and on Cateno is a gradual recovery. If the recovery persists, we are likely to see improvements on Cielo's numbers.

Let me talk about some fronts that we expect improvement inside of Cielo. So first, as I talked about throughout this presentation, we have a different pricing policy for large accounts, we're trying to extract more profitability there, in some cases, the clients are accepting different prices and others are migrating to the competition. So that's part of the business, we are seeking greater profitability.

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In terms of the long tail, we changed our strategic policy and just to share with you how impactful that is because we still carrying the subsidy amortization from last year, but we will not carry that in the next year, because the amortization of subsidies is done in 13 months. So on the first quarter, we have BRL76 million of subsidies. In the second quarter, we had BRL60 million. So that will have an -- in our earnings. We will keep pushing on an efficiency agenda, we are presenting better metrics in comparison to the last year and we are likely to keep seeing that in the upcoming quarters. And we do have another important item to address, which is the performance of our US subsidiary, Merchant e, which is owned by another wholly-subsiary called Cielo USA. Cielo USA, because Merchant e in doing a turnaround process, it still have some costs related to this restructuring process. The loss in BRL is now being magnified by the depreciation of the BRL, the loss that Cielo USA presented in the first quarter was at 54 million.

The loss that is presented on the second quarter was up 87 million. So just think Jeff of the impact in one quarter, the second quarter of adding 60 million in subsidy amortization and also 87 million in foreign Investments. So by combining improvements on these fronts that we talked about the large accounts, the long tail we see gradual cycling through of the amortization of subsidies includes the efficiency and we believe that the turnaround process of Merchant e will be completed by the end of this year and we will be able to have a strategic evaluation of this asset from the beginning of the next year. That's how I look at important improvements that can arrive at Cielo's profitability on the short to medium term.

Q - Jeff Cantwell {BIO 18876343 <GO>}

Okay. That's very clear. Thank you very much. Appreciate it.

A - Gustavo Sousa {BIO 17683157 <GO>}

Thank you, Jeff.

Operator

This concludes today's question-and-answer session. I would like to invite Mr. Paulo Caffarelli to proceed with his closing remarks. Please go ahead, sir.

A - Paulo Caffarelli

Yes, thank you. As you could see this quarter was unusual because the correlation between Cielo and the change in Brazil but I hope that the next quarter we're going to have very good results considering all the things that we are doing on the company relating to our strategy. Thank you all for taking part of this meeting. I hope that we could answer and clarify all the questions. And if you had some doubts or even other questions, do not hesitate to contact us, please. Thank you so much. Have a good day.

Operator

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

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