

Y 2021 Earnings Call

Company Participants

- Guilherme Nahuz, Investor Relations Director and Sustainability Director
- Irlau Machado Filho, Co-Chief Executive Officer
- Jorge Pinheiro, Chief Executive Officer
- Mauricio Fernandes Teixeira, Chief Financial and Investor Relations Officer
- Unidentified Speaker

Other Participants

- Beatriz Abreu, Analyst
- Fred Mendes, Analysts
- Joseph Giordano, Analyst
- Leandro Bastos, Analyst
- Mauricio Cepeda, Analyst
- Ricardo Boitati, Analyst
- Vinicius Figueiredo, Analyst
- Vinicius Ribeiro, Analyst
- Yan Cesquim, Analyst

Presentation

Irlau Machado Filho {BIO 5245099 <GO>}

(Starts Abruptly) operational cycle of a healthcare operator, but we were all surprised in the last month of the year in December with the Omicron variant, that brought additional volume of patients, especially to the ERs and to our test facilities and that had an impact on our MCR. But we were able to reach 76.1% which is even better than the previous quarter and 79% for full year 2021. But only in Q4, we had almost BRL120 million of expenses with COVID-19 patients and we don't expect the same level from now on due to the dramatic drop in the COVID-19 numbers and especially what's going on now in the month of March.

In SG&A, we had 14.4% in Q4 '21, that is slightly above Q4 '20 especially due to the recognition of the collective bargaining agreement started in May a retroactive. But we are now going back to normal levels with the possibility to dilute costs of the recent acquisitions. So the eight acquisitions we did in the year. In terms of adjusted EBITDA, we reached BRL265.7 million down 35.4% compared to Q4 '20, but double that of the first quarter of the year.

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We are very hopeful about 2022 -- having COVID in our past, putting COVID behind us. So Jorge and I decided, we would speak together to give you an idea of the magnitude of what we have in hands. This is a company with a net revenue combined of BRL22.5 billion a year, 8.7 million healthcare members. This number, I mean, the second ranking company doesn't have half of that. We have an unbeatable scale and a national footprint. This is a new landmark in the history of the country having a company of this magnitude working throughout the whole country.

In terms of dental members, we have 6.5 million, that's very robust. And cash MCR in Q4 of 70.5%, but we know that, this is going to go down. And for the full year of 2021 that was 72.3%. And adjusted EBITDA of BRL659 million in Q4 and BRL2.2 billion for the full year of 2021. A company of an amazing volume that will go back to normalcy and healthcare provided and COVID-19 costs being reduced now, this had a huge impact in 2021 and we will now go back to the growth levels that we experienced in the last eight years.

You have the floor back, Jorge.

Unidentified Speaker

Thank you, Irlau. Good morning, everyone. Well, I think that we should now move on to Slide number 6. Jorge and Irlau have given us the main highlights of the quarter and full year 2021. And we are now kick-starting this new journey of the two companies combined. But I would also like to draw your attention to the past trajectory of both companies. I have no words to describe what this image can tell us. These two companies are extremely focused. And in the last five years, they both had very robust growth above 24%, 25%. Both of them able to explore their markets, making the most of opportunities and capture in either through organic growth or acquisition all of those opportunities and with an extremely sustainable result and that's the trajectory.

If you look at the right hand side, the bars here show the trajectory that inspires us to seek for more. I can tell all of you who are here today that there is not one single person in the company that is not completely engaged to continue such a wonderful trajectory.

And why is that? Well, the reason why is on Slide number 7. The company makes available the most complete healthcare structure in the country. Number one, by far and that goes way beyond our 84 hospitals and 7,000 beds. This is indeed a holistic view of the healthcare industry that we have, since it covers primary healthcare through clinics, offices, telemedicine visits. Telemedicine has been an extremely important tool and it also covers our walk-in emergency units with a high degree of resolution, our diagnostic centers, clinical analysis, labs that are constantly being enhanced and evolving.

Right now we have nine hospitals being built. From the planning phase to the last stages of construction. So, if we look at the map of Brazil, you will see that our national footprint covers almost the whole country. Actually 92% of our GDP in this infrastructure with our 70,000 employees, thousands of doctors, nurses and dentist. So are the ones that are going to be able to deliver the growth we expect for the coming five years.

So Irlau, I was talking about the sustainability of our numbers of our result, our profitability, and now I would like you to talk a bit about ESG.

Irlau Machado Filho {BIO 5245099 <GO>}

Thank you, Marcelo. These were great comments. I have talked about this in the past, ESG is a topic that is very close to my heart, it matters a lot to me. I'm a conservationist. I'm involved with the conservation of the environment, wild fauna preservation, I'm completely engaged and committed to this. So I was extremely happy to realize right at the beginning of the relationship with Jorge, and when we were starting to combine our companies to see that this is also something very alive with in Hapvida. And together, we'll be able to advance even more in that area.

Let me give you some highlights for both companies. We have an important program on diversity with affinity groups that have been set-up are being interviewed and coordinated so that we can have an increasingly inclusive environment. And we are now part of some important indexes. Hapvida has been included in the FTSE4Good Index and we are now part of the B3 carbon efficient companies index. We had the carbon disclosure project, we got to a B minus and this project is now going to start representing our company through this ESG committee, that I participate in and coordinate. So we're going to start the same process at Hapvida right now. In terms of energy efficiency, we had many partnership, partnership with EDP to build solar farms that is equivalent to a 1,800 houses and will not emit 2,360 tons of CO2.

We are on the right track. And the diversity journey at Hapvida was strengthen with the joining of the LGBTQIA+ Forum joining, and the UN Women and the Social Inclusion corporate network. We have done our greenhouse gas protocol, inventory contemplate in all of GNDI's units with an external audit. And for the first time in history we have offset a 100% of our emissions. So we have become a carbon-neutral company. This is something that will be implemented in Hapvida as well.

Now as a combined company, we're coordinating all of our efforts related to governance, social activity and environmental protection in a unified way. The strength of our company 166,000 employees, 84 hospitals all working together with the same philosophy in mind to protect what we have in hands from the perspective of ESG. And this is going to make all the difference in the country. We are a citizen company of Brazil and of the world as a whole.

Mauricio Fernandes Teixeira {BIO 19758664 <GO>}

Good morning, everyone. In that coming slides, I'll give you further details of Hapvida's results without the consolidation of GNDI's numbers since the closure of the operations happened in February, actually on February the 11th. The teams are working together to consolidate the numbers to present the variations and analysis of the first quarter of '22 of the combined company in our next earnings release call.

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On Slide number 9, you can see the variation of Hapvida's revenue and its main growth drivers. Net revenue in Q4 '21 grew by 14.3% when compared to Q4 '20. And the revenue for the full year of 2021 grew by 15.5% vis-a-vis 2020, mainly driven by the organic growth of 87,000 lives in healthcare and 186,000 lives in dental in the year. In the last quarter we had a growth of 34,000 lives in healthcare and 73,000 lives in dental. These are the numbers of organic growth, excluding the churn of the recently acquired Premium and Promed. This was also influenced by the client portfolio of the consolidated companies in Q1 '21 with 10,000 lives of Samedh and 11,000 lives of Plamheg. And the revenue coming from the acquired companies Medical Sao Jose, Promed and Premium that did not exist in 2020. And also the growth of the medical and hospital services provided to third-party and company's (inaudible) and Maida Health our healthcare.

Now talking about cost. On Slide 10, we have our COVID-19 related service curve. As Jorge said in the beginning, there was a significant increase in the number of visits in the second half of December due to the dissemination of the Omicron variant in Brazil, together with an influenza epidemic that impacted Q4 as well as the month of January and February 2022. But in March, we had a normal level -- normal month with baseline volumes of visits throughout the month. But this third wave of COVID did not lead to an increase in admissions unlike previous waves. So we had a lower impact on costs compared to previous waves of the pandemic.

On Slide 11 in the chart at the top you can see the composition of our MCR in recent quarters on the left hand side and of the year on the right hand side. Our cash MCR in Q4 '21 was 64.9% and 65.2% in 2021, a 5.4 percentage point increase year-over-year and a drop of 3 percentage points quarter-on-quarter. The main impacts on MCR were the increased volume of service to the dissemination of the Omicron variant and the influenza epidemic happening at the same time. And in the fight against COVID, we had additional expenses with personnel, materials, drugs, localization and working third-party services in our own network and costs of our accredited network, a total of BRL14.3 million in Q4 '21 against BRL27.8 million in Q4 '20. And for the year it was BRL349.1 million in 2021 and BRL127.2 million in 2020. The negative readjustments of individual plans had an impact of BRL31 million in Q4 '21 and BRL56.8 million in 2021.

We also had the higher level of MCR of the acquired companies Medical, Sao Jose, Promed and Premium, that are making up the consolidated numbers of Hapvida in Q4 '21 and full year 2021, but that were not present in the comparative period. The MCR of the recently acquired companies is in a downward trajectory due to the integration and standardization of procedures initiatives, respecting the seasonality of the quarters.

Premium and Promed that together had a cash MCR of 86.6% in Q4 '21. Medical and Sao Jose before been incorporated they had a cash MCR of 78.3% and they are already going into the level of MCR of the mature operations. We have an increase of 8.8 percentage points on the cash MCR of the year is explained by the temporary suspension of elective procedures in Q2 and Q3, 2020, which did not happen in 2021, which offset the higher levels of MCR of the acquired companies. That benefited the MCR numbers of 2020 distorting the comparison with 2021, which was impacted by the factors I just mentioned.

On Slide 12, we have a simulation of what would have been our cash MCR had with this considered the extraordinary effects of the period, which are the additional COVID expenses of BRL14.3 million in Q4 and BRL349 million in 2021, the higher MCR levels of the acquired companies and the negative readjustment of individual plans. Excluding those effects this rate would have been 61.2% for Q4 '21 and 59.5% for full year 2021, in line with our historical MCR.

Now on Slide 13, I'll give you a breakdown of the provision for SUS reimbursement. In Q4 '21 we received a new lot of ABI and invoices. The net impact of the SUS reimbursement provisions in Q4 was BRL24.1 million in line with the expectations of a normalized collection flow. For the year the provision was BRL186.2 million.

On Slide 14, you can see the percentage of the SUS reimbursement provision that has been dropping compared to the total medical cost of the company up until Q1 '21. The cost of the company and the second quarter of '20 and the third quarter of '20 was extraordinarily lower due to the suspension of the elective procedures in our network. And so the percentages went up. But considering the ABI we received this quarter that of number 88, about the procedures that happened mostly in Q4 '20, the nominal amount similar to that of the last 15 quarters.

On Slide 15, you can see our operating expenses. Our selling expenses was of 8.4% in Q4 and 7.3% in 2021, an increase of 1 percentage point and a reduction of 0.5 percentage point respectively compared to the same periods of the previous year. The main impact was the deferred expenses of net commissions related to the incorporation of Hapvida of the operators that were part of the Sao Francisco Group. The duration of contracts of the Sao Francisco Group is longer, and therefore the selling expenses were deferred for longer. After incorporation the deferred selling expenses of the acquired companies have started to be paid more quickly since the average duration with Hapvida is shorter.

The administrative expenses rate was 11.3% in Q4 '21 and 10.5% in 2021, a 2.2 percentage point increase and 0.9 percentage point increase respectively compared to the same periods of the previous year, impacted by the collective bargaining agreement, hiring of new employees, and labor indemnification, provision for fiscal risks, labor risks and civil risks, and an increase in expenses with traveling and accommodation due to the return of corporate traveling.

On Slide 16, you can see our EBITDA, Ex-LTIP of BRL394 million, a decrease of 8.8% compared to Q4 2020. The EBITDA margin in Q4 was 15.2%, a 3.8 percentage point reduction in the same comparison. EBITDA Ex-LTIP of 2021 amounted to BRL1.5 billion down 26% compared to 2020. All the comparisons in the reductions compared to previous year are mostly explained by the impacts of the pandemic on our business as we explained earlier. Excluding COVID-19 related medical costs of BRL14.3 million in Q4 and BRL349 million in 2021, our EBITDA margin would have been 15.7% in Q4 and 18.7% in 2021, still with the negative impact of the Promed and Premium acquisitions on the negative readjustment of individual plans.

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Adjusted net profit totaled BRL347.1 million in Q4 '21, a reduction of 51.5% compared to Q4 '20 and a BRL1 billion in 2021 reduction of 11.8% compared to the same period the previous year.

Now on Slide 17, you can see our free cash flow ex-acquisition, which was negative BRL109 million in Q4 '21, impacted by the reduction in EBITDA, was reduced by BRL43.4 million. And the negative variation of our working capital and an IBNR variation of BRL22 million as well as the time to recognize our own medical cost in the (inaudible) and writing-off of bonds of the acquired companies. Also the negative impact of the payment for the property of hospital Viventi in Brasilia and amortizations related to our business combination.

Finally, we would like to highlight that we are making the most of the opportunities in the market to re-buy shares and generate value to our shareholders, because we believe that the current price of our share does not reflect all the value of Hapvida. In Q4, we repurchased 18.1 million shares and in 2021, 23.2 million in shares.

We are now available for questions.

Questions And Answers

Operator

We are now starting the questions-and-answer session for investors and analysts only. As a reminder, if you wish to pose a question please click on the Q&A box at the bottom toolbar and write your name, company and language to enter the queue. When your name is called, you get the request to unmute your mic. Please unmute your mic and ask your question. We would also like to ask you to ask all of your questions at once.

Starting with our first question by Leandro Bastos, a sell side analyst at Citi. Leandro, please unmute your mic and ask your question. You have the floor.

Q - Leandro Bastos {BIO 21416405 <GO>}

Hello, everyone. Thank you for taking my question. I actually have two questions. The first one about the commercial part, I would like to hear from you, what do you see in terms of the sales dynamics in the market both of Hapvida and Intermedica GNDI? And now the second question is about the average ticket trajectory. What do you expect for the year and what are your perspectives in terms of passing through price increases? Thank you very much.

A - Irlau Machado Filho {BIO 5245099 <GO>}

Jorge, would you like to start or should I start?

A - Jorge Pinheiro {BIO 20560013 <GO>}

No. Go ahead, Irlau.

A - Irlau Machado Filho {BIO 5245099 <GO>}

Okay. Well, we're very excited about the year, because we think that the competitive dynamics will be quite favorable for a company with national coverage like ours. As we said previously, we have already started developing a national plan. We have the database for that transformation, after sales department already set-up and we are starting to offer this product at a national level. We are very excited about that.

We should also mention that due to the geographic expansion, both Hapvida and GNDI had percentages of large customers portfolio, like a large customer that had 20% of the lives here with us in the Northeast and the other 80% of lives distributor with other companies. But now, these companies will also be able to use our services in other regions of the country. We have also started selling individual plans in the South and Southeast that is another landmark. The product is already available and we're happy with the beginning of productions in terms of passing through prices.

If ANS -- I mean, ANS defines the growth for the readjustment of individual plans and that's also good proxy for corporate plans, and it should be around 15% or 16% for the year. And for corporate plans, we also expect something at those levels, of course, that should be done client-by-client, a very thorough work considering the MCR levels of each customer. So starting in April, we are going to have this readjustments, as Jorge said. So we're helpful in terms of ticket recomposition. Should also be mentioned that in the recently acquired companies were going to re-map the products and that adjust prices in those companies as well.

Now, I turn the floor over to Jorge.

A - Jorge Pinheiro {BIO 20560013 <GO>}

Thank you, Irlau. I think your answer was quite complete. I just want to mention that we are also very excited about the synergies that are being captured in the commercial area. I see that many of the initiatives are already implemented. We have created a national sell with teams already in place and the business pipeline for products that cover the whole national territory and the visits are already happening. Based on recent report in the short-term, a 100% of the pipeline has been already designed and that will generate great growth possibilities for the future.

As Irlau said, the individual is already running, this product was created in a partnership with both teams. Evolving a concept that was already widely used at Hapvida and now GNDI is also offering this product. And so our commercial fronts make us really excited about the future prospects as sources of new revenue by selling different products. From the perspective of ticket, it's important to highlight that the company is continued to implement their action plans to enhance verticalization levels and technological controls, through enhancing systems and integrating the network, so that we can have the best possible cost structure. And as a result, offer the best quality.

In a year in which medical cost meet the whole market, fill the impacts that will give us much more resilience and sustainability to be able to pass through the prices we need.

And on the other hand, to be much more competitive, considering not only the synergies that were generated, but also all of the initiatives that both companies already had in their action plans. So I think that starting in March, having the teams working together, we saw that the pipeline has been quite encouraging.

A - Irlau Machado Filho {BIO 5245099 <GO>}

Just a comment, Jorge, we're working together and the market sometimes forgets that. But we're being working together for no more than 30 working days as a combined company. And in this period of time more than 20 hospitals of our networks were cross accredited. So a significant opportunity of verticalization and cost reduction.

Q - Leandro Bastos {BIO 21416405 <GO>}

Great. Thank you so much.

Operator

Our next question comes from Vinicius Figueiredo, sell side analyst at Itau BBA.

Vinicius, go ahead. Unmute your mic and ask your question. You have the floor.

Q - Vinicius Figueiredo {BIO 20592660 <GO>}

Good morning, Jorge, Irlau, Mauricio and Marcelo. Thank you for taking my questions. My question is about, growth in the Southeast. If we exclude the result because it doesn't make much sense to be commercially active there -- starting to structure your operations. The Sao Francisco numbers affected those consolidated numbers and once you remove the lives [ph] that don't make sense in the portfolio, why is it that does happen just now? And what are you planning in terms of growth for -- in the region, after this one time adjustment that has been in need?

Now my second question, if we exclude some (Multiple Speakers) in the operating (Multiple Speakers). Hapvida grew almost 70,000 live in the quarter, if I did the math right. Why is that? And do you see the same dynamic happening now in the first quarter of 2022?

A - Unidentified Speaker

Thank you for your question, Vinicius. That's a great question. We have implemented systems in three different operators last quarter. Sao Francisco, Sao Jose and (inaudible). Our cancellation was quite low in 60 days. According to the law, we will cancel the users, so that we're not exposed to SUS reimbursement and other things. So as we implemented the systems in Q4 and in most acquired companies, the same thing happened. We have cancelled the plans earlier than expected. Companies usually take 120 days to do the cancellation, but we are compliant with the act and we do the cancellation within 60 days. If you remember, in March last year we had a drop of 30,000 lives in Guyana and America because they canceled only with 140 days. So we remove the non-paying users from our network within 60 days. So we are reducing the portfolio, but

that does not have an impact in the cash flow, because we were only removing users that were bad payers. So once we implement the system this is something that we do automatically.

So there is no impact on cash, but we remove from our customer base the non-paying users with the implementation of that role. And our mature operations are growing well. As you can see, throughout the country, we had growth in Q4. And Belo Horizonte, as you said, we are remodeling our portfolio. We stopped selling in some cities and there are some capital cities in which not -- Hapvida GNDI have their own network. So we're not selling there. And we're also discontinuing some small towns. That for example, there is town in the country side of the state of Minas Gerais and we have a Santa Casa, that was part of our customer base and the MCR was over 200%. So without our own network, using an accredited network, it doesn't make sense to sustain an MCR at those levels. So we are making these portfolio adjustments preparing new products.

And still talking about Belo Horizonte, Hapvida and GNDI have already devised a very robust plan for the city, a plan that enabled us to cut duplicated CapEx that both companies would do. So we rationalized and unified the strategic plan for the city of Belo Horizonte. We have spectacular hospitals there. We're talking about three of the best hospitals in Belo Horizonte. We made the acquisition of an important to land on Avenida (inaudible) and the network of labs and outpatient clinics is now been implemented. So we are preparing the ground for an extremely competitive product that will be made available, considering the geographic distribution in the region and the quality and complexity of the assets there. So we're very happy with the plan for Belo Horizonte, and we are preparing to have sustainable growth there. I believe we're on the right track. We are keeping in our customer base, clients that will give us the opportunity to achieve sustainable growth in the long-term.

Any other comment about Belo Horizonte?

No, I just want to say that I love the city of Belo Horizonte. I was born there. So yes, this city is really important to me. But we're very excited. We have hospitals that are accredited by the Joint Commission in Belo Horizonte, and will have a product that will be extremely competitive after we implement the whole infrastructure, we have planned for the city. So yes, Belo Horizonte will go into this completely new phase with a player -- with a national footprint offering high quality products there.

Q - Vinicius Figueiredo {BIO 20592660 <GO>}

Great. Thank you for your answers and have a great day.

Operator

Our next question is by Joseph Giordano, a sell side analyst at J.P. Morgan.

Joseph, we're unmuting your mic. Please go ahead and ask your question.

Q - Joseph Giordano {BIO 17751061 <GO>}

Hello. Good morning everyone. Thank you for taking my question. I would like to address two topics. The first one more focused on the internal work you're doing. We saw relevant increase of expenses, is this something that is related to the acquisitions? What are the provisions for contingencies you have?

And the second topic, I would like to address is about your broader strategy. How are you looking at the negotiation of customers you have in common? Jorge said that you have some customers that have been working with you in one region and with other operators in other region. So what are your combined agreements in terms of prices?

Now, I would also like to understand, where you are focusing on when it comes to market opportunity? Are you planning to have a lower ticket than the average of both companies combined with the more entry level product? Or are you going to focus on a more intermediate or higher intermediate segment, in which you have a greater presence of Unimed?

A - Irlau Machado Filho {BIO 5245099 <GO>}

You asked about Intermedica, so let me start by saying that both companies have a similar profile in terms of product democratization, that is we focus our product for the -- on the emerging middle class. This has always been our focus and we have always been very successful in doing so. That doesn't mean that in our product portfolio we don't have products for the premium market, we do have that available. One of the things that will be made available is a PPO product for the top management of companies that currently have Hapvida, so we are launching a product for that segment.

Now the business combination gives us the possibility of drastically reducing costs by verticalize an operations, simply because there are locations in which Hapvida has a hospital and GNDI had to buy services from third-parties. But from now on, we can verticalize the service in that city within our group and that strengthens the competitiveness of our product. And there is no doubt that product quality will increase as a consequence, because we will have greater control on chronic disease, for example, or the work that we can do to reduce pre-term labor and so on and so forth.

And there is no question that this will compete with average ticket products at Unimed. And we are going to be more competitive in terms of prices. When it comes to costs, that GNDI indeed we felt the impact of the collective bargaining agreement, we have different unions in different regions of the country. But that collective bargaining agreement happened last quarter. But now we're going back to normal operations maybe after Jorge's comment, Marcelo can give you further details about cost.

A - Jorge Pinheiro {BIO 20560013 <GO>}

Great, Irlau. Just a reminder, the country has less than 24% of the population with the healthcare plan. The three COVID waves that we experienced, that we have just overcome and we should celebrate that. This makes us believe that in the short term our operations will normalize, but that makes people want even more to have a private healthcare plan.

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Considering all the trust that people have been us in the care that we are providing with different technologies. And I think that the combined company is now have around 400,000 telemedicine visits a month -- 360,000 telemedicine visits a month.

We are offering a network that has national coverage, that provides comfort to users. And the beauty of those combination is the wide range of opportunities and gains that will be generated. And through these different initiatives all the gains are being mapped and captured. And part of that will be given back to users with smaller price adjustments, given greater predictability to our customers and being the top choice to get to the other 76% of the population, that is not covered by a private healthcare plan.

And we have this wide range of products, but of course I have to say that the main product we have is the combined network with a national footprint that's the main attraction of our company. In all major cities you have Hapvida and GNDI's hospitals, labs, outpatient clinics and of course we want to enhance and expand that even further. But we have Hapvida, we have three products: our plan, the mix and the premium, with a more open network for diagnostics and other hospitals. And GNDI has the BPO [ph] product that will be offered to customers that already have Hapvida and want to have a free choice plan to part of their -- effort to part of their employees. So this is a great opportunities of synergies and that will make our product increasingly better, increasingly competitive and with an enhanced geographical coverage.

Now, I turn the floor over to Marcelo.

A - Unidentified Speaker

Yes, yes. You talked about our G&A, Joseph. And I just want to emphasize that if we look at the annual results, we had a significant decrease of 0.7 percentage points going from 9% in 2019 to 8.7% and now from 8.7% to 8%. So I think that our commitment and our efforts to dilute our G&A as we expand our operations is a constant challenge. And of course we have quarterly variations that are completely normal. And I can tell you that the two variations we had in Q4 are not expected to last.

When it comes to contingency and ANS fee that was something isolated for the restructuring of products in new locations and closure of certain products, so that we could focus on launching the Connect product in the South region and in Minas Gerais. So you also have some marketing fees associated to that. And of course, personnel, we had the collective bargaining agreement with -- and we also had a correction of provisions for vacations, 13th salary and so on and so forth. So you usually have a higher impact in a certain period of time, but we're committed to continuing diluting our G&A.

Operator

And our next question is by Vinicius Ribeiro.

Vinicius, we are going to enable your mic, please unmute and ask your question.

Q - Vinicius Ribeiro {BIO 19720178 <GO>}

Hello. I hope you can hear me? Thank you for taking my questions. So I would like to follow-up on something that Irlau commented about this cross verticalization so to speak. At different times, the expansion in both companies, you had to expand your network and increase your footprint in terms of the service network. So I just want to understand in light of the additional demand that your national plan will bring about, do you feel like you need to adapt or structure or the existing structure is enough to cover that new demand?

And now second point, should talking about your national plan. When we think about price and verticalization level when compared to the baseline of both companies, should we expect that the national plan will bring lower tickets or should we expect a similar pricing to what you have today? And that will generate additional efficiency to you.

A - Irlau Machado Filho {BIO 5245099 <GO>}

Jorge?

A - Jorge Pinheiro {BIO 20560013 <GO>}

Okay. I'll start. Today we have a product that we can call national product because it is present in all main regions of Brazil with our own network. But naturally I don't have the exact numbers, but this is a product that is present in over 86% of the Brazilian GDP. I think that's the exact number. So with our own network we'll be present in all of the locations where we have the greatest income concentration in the country, so the largest consumption market.

So, now with both networks, yes, we can offer a national product present in all five regions and in almost all resilient capital cities and other major cities. But of course this is not a product that will have our own network available in every city in Brazil. That's going to be unattainable and inefficient to have our own network in every Brazilian city. But we have a huge competitive differential here because of the geographic coverage that we currently have. Once again, I would like to emphasize that both companies are working really hard to expand our own network organically and through acquisitions. I know that GNDI and Irlau can you give you further details later, but they're building seven ERs. Hapvida has three hospitals being built in Sao Paulo, two in the Midwest, three in the North and Northeast regions. And acquisitions that we have announced recently in the Northeast region and in the coming days we're going to open a hospital in Brazilia, GNDI has just announced an acquisition in Rio de Janeiro. So as part of our strategy we are expanding in a consistent way and qualifying thus with better architectural designs at the best addresses, with the best technology, and the best professionals to make our product increasingly competitive and offering something that is not available in Brazil. This is the creation of a new concept with a new product that only Hapvida and GNDI can offer to the Brazilian market.

Now about pricing, this is a bit more complex because pricing depends on the concentration of lives in each region. Of course Brazil is so large and so different in different regions, that the average cost also varies. Medical costs in Salvador, Manaus,

Joinville, Sao Paulo or Rio are completely different from each other. So when we do pricing we need to track not only geographic location but age group, type of product, whether you have co-payment or not. If the user participates or if this is based part of the price or if it is 100% paid by the company. So there are many things that are taken into account during the pricing process. We already have an initiative and both pricing teams are already working together in this national sale, to be able to quote the new products in a speedy way.

A - Unidentified Speaker

Just wanted to add something here, Jorge, thank you for your comment. But, yes, when we develop the network and it's now a national product. And the greenfield pipeline is huge as you said, this is all done to fulfill our goal of verticalizing our services more and more throughout the whole national territory. And while we verticalize, usually the cost depending on the region of the country and the city. When it's done in-house it can be 50% lower than what you pay elsewhere, or even more depending on the location. So that gives us extra competitiveness at reasonable prices.

Well, about your first question, Vinicius, about whether we would need any additional CapEx? In this case, I think it's actually the other way around. Hapvida had a business plan with an approved CapEx and GNDI had another one. Once you combine both, we were able to identify some investments that would no longer be needed. That would generate an excess of network that we don't need. So as a result, we are going to save CapEx money here.

A - Irlau Machado Filho {BIO 5245099 <GO>}

Just to add to Jorge's answer, the combined national structure will be present in a total of states representing 92% of the Brazilian GDP. An important synergy of the cross verticalization is that oftentimes the company has already offer national solutions but they use third-party network or other operators.

Now GNDI has a client in the North, that is served by our partner operator, that is not Hapvida. But now we're crossing the data, so that these customers can now be served by Hapvida and vice versa. This creates huge synergies and we are performing those crossed verticalization of operators and installed network.

Yes, just an example, after the acquisition of (inaudible) in Minas Gerais we had lives in Para, Mario [ph], Manaus, and that is now been taken care of by Hapvida that has local infrastructure to serve these customers at a much lower price than we were paying previously. And we also acquired operators that had lives in Recife, the same happened with Hapvida and acquired operators. And now we can serve all of those lives with our own network.

A - Unidentified Speaker

That was a great point. That is actually one of the initiatives to capture synergies in the short and medium terms. So this is an implementation that's not highly complex, this has

already been mapped. We have our pipeline per city. And in a few quarters, we'll start to see these synergies being captured.

Operator

Our next question is by Mauricio Cepeda, sell side analyst at Credit Suisse.

Mauricio, we are going to enable your mic, please unmute and ask your question.

Q - Mauricio Cepeda {BIO 21783651 <GO>}

Good morning, everyone. Thank you for this opportunity. I have a few questions that go back to some aspects that have already been addressed. The first one about the cancellations. You have had a great gross adds but you still have a high level of cancellations. I understand that you've been cleaning up some of the portfolios, but can you give us further details about other reasons that are leading to cancellations that are not cleaning up of portfolios and when will this trend slowdown?

Now, my second question, since we're talking a lot about verticalization and possible gaps, where are the main verticalization gaps that you have today? Is this impacting somehow your M&A decision making process, a trade off between buying lives or buying infrastructure?

Now two unusual questions, that I will try to ask as one single question. In terms of regulation and legislation, we've been seen that maybe ANS National Formulary can become an example. Have you been able to calculate a possible impact on your actuarial numbers? And now the salary floor for nursing staff, how distant are you from this new value that is being proposed and that could create an impact on your payroll?

A - Irlau Machado Filho {BIO 5245099 <GO>}

Jorge, would you like to start?

A - Jorge Pinheiro {BIO 20560013 <GO>}

Well, these are many different topics to be addressed. While about cancellations, Mauricio, thank you for your question. While about cancellations and we basically have two reasons. System implementation as I said, we are now able to shorten our cancellation deadline. And we are able to remove users that were bad payers. This has no cash impact and we see no change in default behavior. But we are now being more efficient. It's no use having in your database, users that are not active and are at default, but the delinquency rates are stable. This is a one-off effect. After you implement the system and you clean up the portfolio this is not something that will continue to happen.

Now a second thing that we've been doing is to discontinue some regions that don't make sense for us to be present in, because these are regions where there is no possibility for us to implement our business model, considering the population of density they have. And in the local hospitals we don't have a lot of room for maneuver to have our

best management in place. So we are discontinuing those cities, we believe it doesn't make sense to have in our base customers that will not have a positive effect for our operations.

Basically, these are the reasons. But the sales levels are great as you saw. And we can now make these adjustments in our portfolio so that all of the sales done at our company are healthy and sustainable. We are not focusing on short-term results. Irlau and I have been talking about that. Our focus is to have sustainable and safe structure that will give us resilience and high quality of service. And of course we want this to be predictable for users. We don't want to pass through 30% or 40% re-adjustments. On the contrary, we want to be able to offer products that are sustainable and high quality.

About ANS's formulary or list, I see a very low chance of that thriving. One of the main foundations of the agency -- the regulatory agency is to define the list -- the formulary. So if the formulary is no longer working, that would mean closing down the regulatory agency. And they were responsible for making huge advances in the private healthcare industry in Brazil. So I don't see reasons why this should happen. When it comes to the floor of the nurse and staff, this is still quite incipient.

So, first of all, I think that we need to value and congratulate our nurse and staff, they have worked really hard to fight the COVID-19 pandemic and its different waves. So we want to congratulate these spectacular healthcare professionals, that face those on a daily basis. But the discussion in Congress today is funding source for CDs, Santa Casa and other philanthropic institutions. And of course we have the possibility of passing through, in case of any new measure. But we have no defined numbers because this is still very incipient, as I said, and many different possibilities are being studied in Congress right now. And since this is not mature yet, we don't have any specific numbers to share with you.

Irlau, would you like to add anything?

A - Irlau Machado Filho {BIO 5245099 <GO>}

No, just a final comment about this exemplary list. In addition to leading to the closure of the regulatory agency that would also lead to the closure of any actuarial calculations, because you cannot perform any actuarial calculations without understanding the risks. And that would be very counterproductive for the country and for consumers. So a consumers should have a saying this. So I don't think this type of action will have a chance to thrive.

Operator

Our next question is by Fred Mendes, sell side analyst.

We will unmute your mic, so that you can ask your question, go ahead.

Q - Fred Mendes {BIO 22302086 <GO>}

Good morning, everyone. Yes, I have two question. My first question is related to San Francisco. Of course, this is a more complex asset, but you have a deadline of 2.5 years for the complete integration. So can you tell us about the performance of that specific asset? And now a question about GNDI, what can we expect of the new individual product that GNDI has launched in Sao Paulo recently? And these are products that you've been working on for some time, I think so. Do you think that this will have a more relevant impact on the second quarter of 2022 already? Thank you.

A - Jorge Pinheiro {BIO 20560013 <GO>}

Okay. Let me start with Sao Francisco and then you talk about the individual product. Okay?

A - Unidentified Speaker

Sure.

A - Jorge Pinheiro {BIO 20560013 <GO>}

Okay. So as a reminder, the Sao Francisco was the Group was the greatest acquisition that we made. It was definitely challenging, that was an operator that had network and customers in four Brazilian regions. So with very large footprint. And we were talking about an integration deadline of four years, because we were already considering all the complexities, but we were able to reduce that by half. We're able to do the whole infrastructure integration, systems integration and operational integration. Sao Francisco is now 100% integrated into Hapvida systems. All the information we have in Hapvida's mature information is already reflected at the same intensity in Sao Francisco's assets in real time.

So we were able to reduce by half that deadline -- that timeline. So what do we still have ahead for some Sao Francisco? Only the build enough hospitals and the implementation of wider network of our own assets. This is a continuous process but the integration has been completed and Sao Francisco was running with an MCR that was a bit above 70%, but we were able to reduce 5 to 6 percentage points. In this period of time, which is something spectacular with this operation that is partially verticalized. Half of Sao Francisco has their own network and the other half doesn't and probably won't have. We have some projects for hospitals that will increase the verticalization level, that's true. But we already had an amazing game in two years that is half the timeline that we predicted at first. So a very successful integration in that sense.

Thank you for your question Fred.

A - Unidentified Speaker

Now let me tell you how we launched a comprehensive individual product. First of all, you have to train brokers, you have to register and structure your product. This is all based on our own network. Our individual products are 100% verticalized. And of course we need to agree with brokers what the compensation will be. And then we can launch a product, this has already happened, we have already started sales. For a week now, it's been quite successful and we expect us to have gradual repercussions, it's like stairs, you sell a group

of products today and you start with the compensation this month. And then the following month you have the new sales plus what was sold the previous month. So it's like a stair with steps, so we expect the results. These results to have impacts on our earnings in the coming months, yes.

Now individual products also have a grace period. So MCR at first is a bit more timid and the results are even better therefore.

Q - Fred Mendes {BIO 22302086 <GO>}

Yes. Thank you so much now. In theory then, it should have the higher price and a greater margin as the products gain momentum, right?

A - Unidentified Speaker

Exactly.

Q - Fred Mendes {BIO 22302086 <GO>}

Okay. Thank you very much.

Operator

Our next question is by Ricardo Boitati, sell side analyst at Banco Safra.

Ricardo, we are going to enable your mic, please unmute and ask your question. You have the floor.

Q - Ricardo Boitati

Thank you everyone, I hope you can hear me well. I have two quick questions. The first about Hapvida and the fine of BRL15 million defined by ANS. There is a liability of BRL460 million classified as possible. So can you give us further details about what happened there in Q4? And how that compares to this contingency, liability, so that we understand if there is a risk of that happening again or if that was something one-off?

Marcelo commented a bit about GNDI but if you have anything else to say about this, Marcelo. Please go ahead. And when will this provisioning become cash? Because once you recognize this provision today, you have expectations for this to become cash in the next 12 months or not necessarily. I know that this is not as significant, but I just want to understand if there is anything else that can impact your P&L in the coming quarters?

Now, my second question is for GNDI. Just a clarification about the MCR, you said that you had an impact in the demobilization of COVID-19 related infrastructure. Is that related to the COVID-19 care costs or is it something additional?

A - Guilherme Nahuz {BIO 21255437 <GO>}

FINAL

Hello Boiati, this is Guilherme speaking. I will answer the first question about the ANS fine. Well this is a common administrative process just business as usual. We have 72 administrative suites, so it's not a fine coming from one suite, one process. These are diverse administrative fines that we got from 2007 to 2013. So these are old suites. And that was at an administrative level. Now we are appealing against this at the judicial level. Hapvida has already filed the appeal and we are waiting. We don't know when we're going to have a response. But the provision had to be made now because these suites were classified by third-party officers as probable loss.

So we did this provisioning right now of this -- without knowing exactly when this is going to happen. But that's one timer, not a recurring effect. And we are talking about a large volume of old fines and this is part of business, business as usual, nothing extraordinary.

Now I turn the floor over to Marcelo, to answer your GNDI question.

A - Unidentified Speaker

Well about MCR, we said BRL126 million of COVID impact that was the impact of medical costs, medical claims and service cost. Demobilization of assets was not included in those numbers, that would be additional, on top of that. Because that is related to personnel, adjustment, reduction of medical teams to be more inline with our current needs and closure of beds. During COVID, we were opening many new beds and now all of these beds were closed. We no longer have any hospital wards for COVID alone, that is part of the past. We now have gone back to business as usual.

Q - Ricardo Boitati

Okay. Thank you very much.

Operator

Our next question is by Yan Cesquim, a sell side analyst at BTG Pactual.

Q - Yan Cesquim

Good morning, everyone. I have three questions. First, we have noticed a lower level of net addition in the quarter, impacted by a higher churn especially in recently acquired companies Promed and Premium. This cancellation dynamic has been reverted in the beginning of 2022 or not? And number two, how are the sales like in the beginning of the year? Is there an improvement in net additions? And third, when should you start selling the national product?

A - Unidentified Speaker

We'll start by answering your last question. The national product is already been sold. The offer is already been made and we have a sales funnel and which we identify a group of possible customers, prospects, right, and we start visiting those customers. And we are talking about a huge addressable market over 700,000 lives. So we've been talking to these customers and for some of them we are already at a second stage of negotiation.

And some of these customers are already in the signing phase, so this national product is already being sold.

Now about cancellations, in the beginning of the year, we have a lower level because of other expenses that customers have with taxes and school. But we are very hopeful with all the initiatives we have in place. At least the pipeline is making us very excited about the future.

Operator

Our next question is by Beatriz Abreu, sell side analyst at Goldman Sachs. Beatriz, you have the floor.

Q - Beatriz Abreu {BIO 22423197 <GO>}

Hello everyone. Good morning. Thank you for taking my question. I have two quick questions. The first one, about the deferred commission expenses related to the incorporation of the Sao Francisco Group, that had an increase in the quarter. Can you tell us why that happened and what you expect in terms of those expenses in the future?

And my second question is, can you give us some idea about the tax benefits of this premium deductibility? You think there will be an increase in that with the combination of business, what do you expect from now on?

A - Unidentified Speaker

Thank you for your question, Beatriz. About the deferred expenses, what happened was that in Sao Francisco we had a few contracts, and the cost of acquisitions were still being paid for. Now in terms of churn, when we wrote-off those customers, the value to be recognized was written-off from the results, because it made no sense to have that recognized in our results. The commercial expenses of customers that were no longer generating revenues. So we did this one-off, writing-off.

About tax benefits, we've been working a lot with Marcelo and other legal consultants to see how we can optimize tax, considering the added value that was created. And as a reminder, both companies have made acquisitions and they have premiums to be seized, like Sao Francisco was BRL1.5 billion in terms of tax benefit. And that's going to last for a few quarters. So we don't have to launch this new value that was created for GNDI. We also have recent acquisitions and we are planning, how we're going to use that value, to see how we can make the most of it. So, we don't need to be in a hurry when it comes to tax benefits, but to have the low as possible tax level.

And as time goes by, we're planning how we're going to use those benefits that are being generated right now. For cash effects, both companies already have levels of tax that are very low and with a good accumulation of value to be used. So we're now going to plan for the years coming ahead with new incorporations, so that we can keep this very low level of taxes -- effective taxes.

FINAL

Bloomberg Transcript

Q - Beatriz Abreu {BIO 22423197 <GO>}

Okay. Thank you very much.

Operator

This concludes our questions-and-answer session. Now I would like to turn the floor over to the company for the final remarks.

A - Irlau Machado Filho {BIO 5245099 <GO>}

Go ahead, Jorge.

A - Jorge Pinheiro {BIO 20560013 <GO>}

Once again, I'd like to thank you all for joining us today. I would like to thank Irlau and the GNDI team for the welcome. I'm very happy, we are now working together. And I want to thank all of our employees for the huge effort they have made together with us in 2021 and we'll continue to work hard together in 2022 to fulfill our mission, which is to provide high quality healthcare in an affordable way to the Brazilian population.

I would like to thank our investors for being with us, supporting us in our growth. Thank you so much.

A - Irlau Machado Filho {BIO 5245099 <GO>}

Thank you, Jorge. Thank you, Marcelo, Mauricio, (inaudible), everyone, investors and analysts and see you next time.

Operator

This concludes Hapvida's Fourth Quarter 2021 Earnings Conference Call. The Investors Relation department is available to answer any other questions you might have. Thank you very much for joining us and have a great afternoon.

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