Q2 2020 Earnings Call

Company Participants

- Adalmario Ghovatto Satheler do Couto, Chief Financial Officer and Investor Relations Officer
- Breno Toledo Pires de Oliveira, Chief Executive Officer

Other Participants

- Alexandre Falcao, Analyst
- Frederico Mendes, Analyst
- Gustavo Oliveira, Analyst
- Joseph Giordano, Analyst
- Unidentified Participant

Presentation

Operator

Good morning. Welcome to Hypera Pharma's Second Quarter 2020 Results Conference call. Today with us, we have Mr. Breno Oliveira, CEO; and Mr. Adalmario Couto, CFO and IRO. We would like to inform you that this event is being recorded and all participants will be in listen-only mode during the company's presentation.

After the remarks, there will be a question-and-answer session for investors and analysts only and further instructions will be given (Operator Instructions) We would like to inform that questions can only be asked by telephone. If you're connected through the webcast, you should email your questions directly to the IR team at ri@hypera.com.br. Today's live webcast may be accessed with the company's Investor Relations website at hypera.com.br/ir. We would like to inform you that some statements during this conference call may constitute forward-looking statements. The statements are subject to known and unknown risks and uncertainties that could cause the company's actual results to differ materially from those set forth in the forward-looking statements.

Now I'll turn the floor to Mr. Breno Oliveira, who will begin the presentation. Mr. Breno, you may begin your conference.

Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Good morning, everyone. Welcome to our earnings call for the second quarter of 2020. I'd like to begin by talking about the conclusion of the efforts in the independent committee. (Technical Difficulty) we communicated to market that the committee's activities will be concluded.

The Board approved a payment term in which our main shareholder without taking responsibility and understanding this to be the company's -- in the company's best interest as well as its shareholders agreed to pay the company the remaining value of undue payments found by an internal investigation, amounting to around BRL110 million.

The independent committee also presented recommendations aiming to perfecting even further our internal controls in our compliance program, which has evolved significantly in the last years. These recommendations are being assessed and put into practice by our compliance team coordinated by the auditing committee. The company continues to collaborate with the investigations and is assessing legal top -- new alternatives to conclude this situation.

Now we're going to talk about our operational performance on slide three. Our net revenue reached BRL1,050 million in the quarter, 8% higher than the second quarter of 2019. This was boosted by a strong growth in sellout in Consumer Health at the end of March, which did not impact the net revenue in the first quarter. And, as a consequence, the surge that consumers had in buying over-the-counter medications in the beginning of the COVID-19 pandemic and also increased sellout in Generics over the second quarter of 2020.

Due to the challenges caused by the pandemic, we have been having more discipline in managing expenses and costs, which has resulted in an increased EBITDA margin in the second quarter both compared to the second quarter of 2019 and the first quarter of 2020 even excluding other nonrecurring operational revenues.

Social isolation have maintained -- are maintained through the second quarter of 2020, which reduced the number of people in pharmacies, reduced the number of doctor consultations and in the reduction of prescription medication, especially the acute use medication, which is a relevant part of our portfolio that led to a negative impact on the Brazilian pharma industry, and as a consequence, affected our sellout, which had a drop of 1.6% in the quarter.

This was caused mainly by our performance in April. And movement restrictions were stronger in the main regions of Brazil and our medical visiting teams were put on furlough. In April, our sellout dropped by 10%. From May, we saw that social isolation was flexibilized in some regions, which led to a gradual recovery in the number of doctor consultations and increased the number of people at pharmacies.

These factors and the return of the medical business teams and the merchandising teams as well as resuming our investments in point-of-sale and intensifying our investments in digital marketing has recovered our sellout performance. In June, we grew 7%. And based on preliminary data, July will also have a growth of 7% to 8%.

The Generics category was the main highlight of the second quarter. Sellout grew especially boosted by generic medication and brands, Doralgina, Histamin, Dropy D and Centrotabs as seen on slide four. This growth was taking place especially in medium networks and in the regions that were further from the big cities, which highlights our distribution strength, which can reach basically 100% of pharmacies in Brazil.

In Consumer Health, the highlight was once again the vitamins and supplement segment, which has been underscored by the recent launches, Vitasay and Tamarine as well as Biotonico Fontoura and Maracugina. We have to highlight that the anti-flu medication segment, where we are market leaders have presented a strong drop this quarter impacted mainly by social isolation and the winter in Brazil, which is the most important sellout period in this category.

Prescription products were once again benefited by the Addera brand, which gained market share this quarter and is still benefited by recent studies, which reinforce the importance of Vitamin D to regulate the immune system. Beside that, recent launches such as Colflex and Ofolato also had an important performance this quarter.

On the other hand, despite the gradual recovery we've seen in the number of doctor consultations after our teams have come back and after social isolation has been flexibilized, the quarter has been marked by a strong reduction in the number of doctor consultations because of the COVID pandemic impacting sellout negatively in some relative categories such as dermatology, pediatrics and orthopedics.

In the second quarter, we have not lost sight of our long-term objective, which is innovation. We've invested 7.1% of our net revenue in research and development launching some extended product lines, which are important for the company. In prescription product, I'd like to highlight Colflex Trio, an extension of the Colflex brand to treat osteoarthritis, pain and cartilage regeneration and Gestamax Plus, an extension of the Gestamax supplement indicated during pregnancy.

In Consumer Health, the main launch has been a line extension of the sweetener Zero-Cal brand with a new presentation based on Eritritol. Before I let Adalmario speak about the second quarter results in further detail, I'd like to quickly mention recent acquisitions, shareholder payouts and some of the measures we've taken about COVID-19, shown on slide five.

We've taken important steps in acquiring Buscopan recently selling Neocopan. The contribution of Neocopan for our operations EBITDA in 2019 was under 0.5%. Besides that, we hedged all of our exposure to the US dollar in acquiring Takeda brands.

We've maintained our shareholder payout strategy. We declared BRL186 million in interest over our own capital or BRL0.29 per share, a growth of 15% versus the second quarter 2019. We've also continued our expansion project in our solids plant, which should be concluded in September and the new area should be put in operation in early 2021. With that we'll have the capacity to grow especially in Generics and to produce Buscopan and Takeda brands, our products internally.

Finally, we maintained our main initiatives to maintain well-being for our teams and the communities we relate to such as reinforcing Coronavirus prevention efforts in our sites, home office for employees who are in the risk groups and for our management teams. And we've also made telemedicine services available to all our employees and their family numbers. Moreover, we donated this quarter respirators and COVID-19 tests for the Anapolis population, a region where we have nearly 4,000 employees.

This quarter, we managed to expand our net revenues, our EBITDA and our net profit. And we generated demand in some relevant categories for the company such as flu medication, dermatology, pediatrics and orthopedics. And they impacted our sellout growth in the first half of the year and as a consequence, our set goals for this year in terms of net revenue.

We have a robust constant motion plan for the second half of 2020 to mitigate impacts of reduced sales and then on that we've establish new guidances for 2020, which are net revenue around BRL4 billion and a net profit of continued operations around BRL1.3 billion. This guidance is already considering the expected results from Buscopan and will be submitted to the authorities still this week, but it does not include the brands acquired from Takeda.

Now Adalmario will speak about other results this quarter.

Adalmario Ghovatto Satheler do Couto {BIO 20598860 <GO>}

Thank you, Breno. Good morning, everyone. Before going into the second quarter of figures in further detail I'd just like to mention this has not been an easy quarter. It actually never is. But we have had very good results with all the challenges we've had especially when we consider the overall economy and other industries.

This crisis specifically highlights not only the resilience, but also the importance of the health industry especially pharma in aiding and treating, developing vaccines and also the importance of prevention and the concern of the population with having a higher immunity.

Now to speak about our results. We had a growth of about 8% in net revenues led especially by increased volumes of 5% to 3% related to increased prices.

Operator

Ladies and gentlemen, please hold. The conference call will return soon. (Technical Difficulty) Ladies and gentlemen, thank you for holding. We will now continue the Hypera Pharma conference call.

Adalmario Ghovatto Satheler do Couto {BIO 20598860 <GO>}

Hi, everyone, sorry for the issue. Just to continue, we were talking about the growth of our net revenue, which was about 8%. It was mainly boosted by increased volumes of about 5% and 3% versus price increase.

Regarding price readjustments, we had a 60-day delay in readjustment, which was authorized by the government for monitored medication. It was supposed to start on April 1st, but it was enacted only on June 1st. In our case, the impact was lower since most of our portfolio is in the free price category and we have more flexibility in readjusting price.

With that skin cosmetic and supplement prices have been readjusted in April. And medications especially in the over-the-counter portfolio increased for May and the rest of the portfolio in June. The average readjustment was about 6.5%.

We had a great contribution this quarter from consumer health led by our clients' restarting their inventories after a strong demand in mainly all of the current categories in March. There will be higher concentration at the end of the month and also acceleration in the demand for Generics as well as the strong growth in revenue and volumes. There was a reduction in prescription products because of the impact of some categories that in which we have a higher concentration such as pediatrics, respiratory and orthopedics.

Now to talk about costs. We had an increase in our costs especially related to exchange rates. The average exchange rate went from BRL4.24 versus BRL3.74 in the same quarter last year. That is a depreciation of 13%. We also had the impact of an effective increase in the dollar price inputs and additional expenses related to COVID and shipping since we have to change from sea transportation to air to increase the availability of the (inauidble). With that our gross margins were slightly below 66%, a reduction of 2.5 points versus the second quarter of 2019.

Before we talk about expenses, I'd also like to mention that not only did we complete hedging to pay for the Takeda acquisition, as Breno said, but we also hedged 100% of our expected purchase in imported inputs for the rest of the year at an exchange rate under BRL5. We also started a hedge for the CapEx forecast especially related to machinery importation to expand our plant.

Speaking about expenses, despite the reduction we had in travel and vehicles in the trade and merchant teams, we had a slight increase versus the same period last year especially because of a higher investment in R&D and expansion in our employees list and materials related to developing new products.

With regards to marketing, where we allocate most of our investments, we optimized management, which has allowed our marketing expenses to be below 18% of our net revenue. We reduced our expenses with media by 17% and we also had lower number of medical events because of COVID-19. We also anticipated vacations for the medical visiting team in April and it normally takes place between December and January.

SG&A was in line with what we had and we had an additional revenue of BRL107 million which came from the damages agreement and payment term between the company and its major shareholder. Depreciation was in line with the previous year.

And with that EBITDA reached BRL440 million or 43% of our margin before nonrecurring expenses. That would be BRL347 million adjusted or 33% of the EBITDA margin. This margin is higher than what we have in our budget due to a slightly higher gross margin, but especially because of the lower investment in marketing.

Financial results were impacted by the additional leverage spread, which we took to reinforce the company's liquidity between the end of the first quarter and the beginning of the second quarter. And we also saw the positive effect of mark-to-market of the hedge related to the Takeda acquisition.

Income tax expenses were about BRL3 million after deducting benefits of interest over our own capital and the sub venture in the state of Goias. With that, our net profits for continued operations were BRL399 million with a total net profit of BRL396 million.

Now let's talk about cash flow. The cash generated by the operation this quarter was more than enough for our CapEx investment especially increasing our productive capacity and maintenance. And it also allowed us to improve our R&D investments to develop new products, generating at the end of the quarter a free cash flow of BRL239 million.

As we have said in the previous call, we spent about BRL2.5 billion in long-term financing in particular to pay for the Takeda acquisition and to make sure that the company had cash resources available. We also took BRL300 million in additional financing to reinforce the company's liquidity. With that we concluded the quarter with cash position above BRL5 billion, which is more than enough to pay for the Buscopan and Takeda acquisitions.

Without considering that those acquisitions, the company still have net cash of BRL370 million. And even after paying for the acquisition, our leverage ratio should be below two times considering the combined portfolio with Buscopan and Takeda. In our balance, the main variations were what we mentioned on the company's liquidity. We concluded the quarter at a comfortable position of over BRL5 billion in cash with an increase of our short- and long-term credits.

Regarding the main ones impacted by our working capital investment, we had an increase of BRL300 million in accounts receivables, which was reflected in the number of days from 95 in the second quarter of 2019 to 110 days. We also had an increase in the level of our inventory, which was offset by the increase in the average return for suppliers. With that, our working capital investments as a percentage of net revenue was stable under 40%.

Now Breno will now give his closing remarks.

Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Thanks, Adalmario. The Brazilian pharma industry has proven once again that not only does it count with several growth opportunities in several segments, but also it is solid and very resilient.

This quarter was strongly affected by the reduction in the number of doctor consultations and the lower number of people in pharmacies that as the main reason as Brazilians resume its activities, our expectations are that the market will gradually go back to its historical growth level especially given the aging population, which favors the increase of the consumption of medication.

Combined with these factors, the strength of our brand and our distribution reaching 100% of pharmacies across Brazil and the conclusion of the recent acquisitions will leverage our sellout growth in the next quarters and years.

Thank you and we'll now continue with the questions-and-answer session.

Questions And Answers

Operator

Thank you. The floor is now open for questions from investors and analyst. (Operator Instructions) The first question is from JPMorgan, Mr. Joseph. Please continue sir.

Q - Joseph Giordano {BIO 17751061 <GO>}

Hi, everyone. I'm sorry, I can't hear you very well, but my question here is on M&A. What is your outlook on potential acquisitions after the recent one you have. I'm sure that given the current context many companies have had troubles with the delayed increased prices and weaker sellout for the quarter. So my question is about your sellout. What do you see are the main trends here for sellout so far and profitability? Thank you.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Joe, we're hearing that the call is not having very good quality, so I'll try to speak slower. I can hear you fine now. Okay. So I'll answer your question and if there are any problems please let me know. So to answer your first question on M&A, our focus right now has been in integrating the recent acquisitions we had.

Q - Joseph Giordano {BIO 17751061 <GO>}

I'm sorry, I can't hear your answer.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

That's okay. Just give us a second and we're seeing what we can do with our provider. So I'll try speak slowly and we'll see if you can hear me. Starting on M&A, our focus right now is to integrate the recent acquisitions we had, Buscopan and Takeda.

We're also focusing on organic growth, innovation, which is the company's main focus. With regard to other opportunities just as we have these opportunities here, we are looking for opportunities that would make sense from a strategical point of view.

From a financial point of view, as Adalmario said, despite the acquisitions, we're still at a very comfortable situation financially. We're expecting a average of two times the EBITDA or under even after the acquisitions. So to summarize, we're going to be looking for opportunities that do make sense from a strategical point of view, but this is not our priority.

With regards to the sellout trends, as I said, this has been improving gradually and slowly. So we saw that the results were negative in April. In May, they were about even. And in June we already saw some growth. And data from July are also showing high single-digit growth levels. So we believe that as social isolation reduces, demand will bounce back again.

And our portfolio, which has been affected especially the influenza and chronic or excuse me acute use medication will recover their demand. We believe that this is a one-off. The second half of next year will not be related to this year assuming the situation with COVID-19 is normalized. This entire trend will be reversed later on. We're looking at the situation on a monthly basis and it has been improving especially in these markets I mentioned.

Another point to highlight here is the performance of the Generics segment, which has been growing significantly. We expect this to continue to grow especially because of some factors. The common consumers are finding alternatives that come at a better cost and also social isolation being reduced. I think social isolation will be reduced in main cities and I'm not sure if that is an answer that you can understand that you could understand.

Q - Joseph Giordano {BIO 17751061 <GO>}

We have some trouble with the connection, but I did manage to hear most of your answer. If you can tell us a bit about your SG&A reduction. You mentioned marketing, but I'd just like to understand how that went on the corporate side, if you had pay cuts, if you reduced your personnel. If you could you tell us a bit about that? Thank you.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Right. Before I answer I just got some feedback saying that the connection is better on the webcast. So if you can connect through there, I think, it will make it better.

To answer your question, Joe, we did not reduce working hours or salaries. We've taken some measures such as a hiring freeze. We've also adjusted some administrative expenses, but many of the expenses were reduced naturally, as Adalmario said, by reducing travel expenses from our sales team, the administrative staff, the reduction of number of free samples distributed because everyone was on leave in April.

Therefore events many of the sponsored events were held online. And with that we also had a high level of savings. And there were some other measures in which we were able to contain expenses more rigorously, but we did not have to reduce working hours. Our focus was to generate demand and that includes the medical visiting and merchandising teams. And I think that's how we're going to be able to recover the demand for our products.

Q - Unidentified Participant

Good morning, Breno and Adalmario. I hope you can hear me well. I can barely hear you. I'm going to ask you my question. The fact that you hired an investment bank for one of the brands you're purchasing, but that -- is that an indication that you're talking to the authorities. Do you think that process can be accelerated. I'm asking about Takeda. You mentioned in your guidance that your expectation was to conclude this by next year. Is that the expectation we should maintain and what did you learn from the crisis. What's going to be better in your operations. I imagine that we're going to see a permanent reduction in traveling and visiting that could generate some savings. So talk a bit about what you learned in the last few months? Thank you.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

So to answer your first question, the Takeda process is going according to our original expectations. So when we announced transactions, we mentioned that we expected to conclude Buscopan on the third quarter and Takeda in the fourth quarter.

So this is still our best estimate. But probably, Takeda, will be concluded by the end of the fourth quarter. Our goal is to have the authorities approve it still this year, so that we can close it this year and have resources of these acquisitions from 2021. That's our best estimate right now.

About the lessons learned and improvements, we think the technology is here to stay especially in what concerns office dynamics as not only our office, but many others. We have acted quickly to the new reality and we think that this is here to stay. So travel expenses, for example, for the rest of the year, they will be cut by more than 50%. So basically we can save on traveling and have online meetings.

This doesn't apply so much to the field team, but our own teams interacting with plants, Sao Paulo, Goiania, Anapolis that was reduced significantly. Regarding medical business, we also take the decision to stay. It should happen from now on. It's a hybrid model to generate medical demands.

So reps can have personal visits, but we can also use tools to visit remotely that can be used to visit doctors again to reinforce the first visit and also visiting doctors in regions we are not present or we don't have a local team.

So that, we believe, is going to stay, and we should see a reduction or that is an increased productivity in these teams by about 30%. This is what I can tell you. I think that's going to be the long-term impact from the lessons learned at this moment right now.

Q - Unidentified Participant

Thank you. In the first quarter, you mentioned you have made a partnership with Rappi, the delivery app. So what else has evolved in digital online sales. You mentioned an accelerated investing in technology companies. So if you could tell us a bit about how that has evolved in this quarter?

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Right. That's also an important point. I didn't mention it before, but we have been working in online sales platforms especially the ones belonging to our clients. So retailers have received investments from us. We have a dedicated team to online trade marketing for our clients and we've increased our investments there and we have been seeing the results.

Our goal is to gain market share and to lead in our clients' online platforms. And we're also working on our own direct sales platform. We launched our own e-commerce platform in the second quarter. And it was only a pilot project with acute res, but our intention is to work on both fronts especially with clients. Some of our clients already have their own platforms and they have a natural demand for these pharma products.

Q - Unidentified Participant

Great. Thank you, Breno.

I'm not sure if they announced my name, but I'll continue with my question. I'd just like to hear about how you are dealing with the demand in June and July. How do you see this dynamic in what you described in the release, the media networks and the meds from the areas that are further from big cities. Do you see that trend still and the second question is, how we should consider inventory and sell-out and sell-in trends in the gap? How that's going to be for the rest of the year? Thank you.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Yes. To answer your first question, we saw this trend moving away from the cities especially at the beginning of social isolation restrictions. As that evolves, we're seeing that we're going back to normal as we had before and this is happening gradually.

To answer your question on inventory, for the first quarter, we finished with an inventory that was slightly lower than expected. As we said, we received a great demand at the end of the first quarter. And now we see that inventory levels have normalized considering what we see happening in the second quarter, estimated growth we saw right now. So our clients and we ourselves have been getting ready for the demand levels that we expected for the second quarter. So the tendency is for this to normalize.

Q - Unidentified Participant

So you're saying that channels are normalized?

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Yes, that's right.

Operator

Our next question comes from Alexandre Falcao, HSBC Bank.

Q - Alexandre Falcao {BIO 5515455 <GO>}

Thank you for taking my question. Actually I just wanted to talk again about commercial expenses and how you are repositioning the company effort to recovery. If you could give us some more color on that. Are you only redirecting expenses for the online channel to reduce expenses at point-of-sale or are you going to dilute your marketing costs? Thank you.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Investments at point-of-sales, it specifically will not be reduced as a percentage of the revenue. We're adapting to the new revenue level that the company expects to have in the new scenario, but our intention is more to reallocate and this packaged our expenses for online initiatives.

This was something that we were not focused on before the pandemic and we now have by creating a specific team in the company. But the idea is not to reduce our total investments in point-of-sale as a percentage of the company's revenues.

Q - Alexandre Falcao {BIO 5515455 <GO>}

Right. If I can ask a follow-up question. Does that mean that when you start having more online sales or more investments in that channel? Will you start looking not only at selling to your clients over this platform, but also providing logistics or would that always be done by your clients?

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Well, as I said, we have a pilot project for direct sales especially some of the categories in our portfolio such as cosmetics and vitamins. But we don't see this as our main channels. It's more of a learning experience, so that you can understand how it works.

What we've learned from others is that online sales will be a small share of our sales. Our main focus will be working specifically on reducing our advertising expenses and that's getting back to digital. But this will be especially directed towards our clients' e-commerce platforms.

Q - Alexandre Falcao {BIO 5515455 <GO>}

I understand. Thank you.

Operator

Our next question will be asked by Mr. Gustavo Oliveira from UBS.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

Thank you. Good morning, Breno and Adalmario. I have a couple of questions. First, about promotional points. This quarter went up, but less than the record. This is helping in conversions. Can you tell us what your expectations are for promotional discounts in the future. Secondly, your gross margin, you've shown that about 50% of your lost margins came from the exchange rate. So I just like to understand where is the rest coming from. Is it the mix and how do you think that will do in the future. And as I said, I'd just like to confirm, I think, as Adalmario said that the average exchange rate for products sold were BRL4.4 in this quarter. I'd just like to understand if that's the same value if I have the right value? Thank you.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Hi, Gustavo. This is Breno. I'll answer your first question about discounts and Adalmario will answer your second. So with regard to discounts, I don't know if you remember, but last year, as we focused on sellout, we were very aggressive especially in some categories such as food medication. And this was done in discounts so that we could increase our sellout. Now for 2020, we also have a mix of the business that is much better balanced.

So we're reducing discounts and increasing medical visits and also investments in points of sale. So that will be the trend for the year as a whole. So what we expect for the second half is to maintain that. You will probably see more medical visits in comparison to last year, a reduction in commercial costs and you'll probably see our sales agreements go up. Adalmario will now answer your other question.

A - Adalmario Ghovatto Satheler do Couto {BIO 20598860 <GO>}

So about gross margins. It dropped by 2.5 this quarter. Exchange rate will be close to 50% of that reduction and the other half was basically the increase in input costs in US dollars. And of course there was increased cost of shipping and some additional costs that we had because it's COVID-19.

So hiring additional personnel to replace those employees who were on leave, buying thermometers and other expenses that we had for prevention in our plants that also impacted our costs. Our mix was not impacted, although we had a higher sales in the Generics category. Among our products, we also had higher sales in higher margin products.

In our brands portfolio, we also have more products that have higher margins than the average of the company such as Addera and also the Consumer Health portfolio. So it was overall a neutral mix this quarter. And the exchange rate this quarter was really an average of BRL4.24. So that created two effects. First, if you look at the average exchange rate for the year, it was around BRL4.8, BRL4.9.

But the exchange rate impacts our cost and our inventory. We accumulate some inventory over time usually four to six months. That's our lead time. And we also hedge. So we have had a better hedging position from the beginning of the year. Up to June, we had hedged most of it at 4. -- at BRL4 to BRL4.1. And from now until the end of the year we are also 100% hedged. I'm not sure that answers your question.

Q - Gustavo Oliveira {BIO 15129435 <GO>}

It does. Just to follow up on your answer. This increased cost of some inputs priced in US dollars, do you think that's structural or was that because of what happened earlier this year? When companies were afraid they won't have enough product. I think in China they also had some issues with logistics to ship products. I think maybe their manufacturing capacity was also not completely used. So do you think this has been reversed? And also about the extra costs you had in your plan, how do you see these variables?

A - Adalmario Ghovatto Satheler do Couto {BIO 20598860 <GO>}

Regarding additional costs, I think, it will depend on the curve we will see as cases go down. But we know that in some areas of Brazil, especially in Goias, we're seeing cases go up. While in some places like Sao Paulo, cases are going down.

So it really will depend on the curve, when the curve will reach it's peak and when it will stop going up. But we have taken several measures to take care of our employees' health. We've implemented more and more measures and it will depend on that curve.

Regarding inputs, what we've seen also is an increase in costs. In China and in India there is a place and different periods. In India, they had a full lockdown and that impacted our production. So we had a delay in their deliveries and this ended up generating higher costs, which were passed on to that for final price. So our supply team is doing excellent work to be able to renegotiate these prices.

Although we had an increased price records, we also got better payment terms. So that makes things easier for us. We have some more days to work with, but we are working to reduce these costs that were increased in the second quarter.

Operator

Our next question comes from Mr. Fred Mendes, Bradesco Bank. Please continue sir.

Q - Frederico Mendes {BIO 19832788 <GO>}

Good morning, everyone I have two questions and I apologize if I ask a question that has already been answered. I had some audio trouble. So I apologize in case if I do ask something that's already been asked. So now we're seeing some pharmacies be more vocal about increasing their own brand penetration where they have (inaudible) better margins. What is your opinion on that? Is that a concern for you that's going to create an impact? And there was a mismatch between sellout and sell-in. So do you think that will impact your results for the quarter as well? Thank you.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Fred, about own brands, this is a movement that we see retailers trying to make for a long time especially starting with personal care and now we see some categories of medication. From our point of view, in the medication category, it's much more difficult to do that. First, because the cheaper option already exists for consumers, which are the generics.

So I think retailers will not have a competitive advantage in comparison to that. We see a slight increase in vitamins, but we don't see that, that will be significant. It started many years ago and it hasn't really become significant as it could be. Abroad, you see this clearly, for example, in the United States. But there's a difference because they don't have the engineering market there.

They have brand or reference market, which have a media behind them. And they have own store brands, which basically cannot be done and result in the same way as done in the US because they basically copy. They have the same packaging as the reference product and the law does not allow for that here in Brazil. So we're looking at that. We've been analyzing it, but we don't believe it will change how the market behaves radically.

We're used to competing with generic versions of our products. We have our own generic lines. And we compete in price, but we don't think that retailers have a price advantage because we know that medication is more complex, it's better regulated. Even these suppliers don't really have a competitive advantage in terms of price.

To answer your second question, I think, the second or excuse me the third quarter will really depend on how sellout develops during the second quarter. We are expecting mid single-digit growth in sellout. And if it's higher than that, we don't think it will have a major impact on our performance.

Q - Frederico Mendes {BIO 19832788 <GO>}

Great. Thank you.

Operator

We now turn the floor to Mr. Breno for his closing remarks.

A - Breno Toledo Pires de Oliveira {BIO 17653260 <GO>}

Thank you for listening in everyone. I apologize for the connection issues we've had, and we are still open. If anything was not made clear especially because of the connection, we're open for further questions. Adalmario and I and the Investor Relations team can answer any questions on the results we discussed today. Thank you, and we wish you all good health.

Operator

This concludes Hypera Pharma's conference call. Please disconnect.