

Y 2017 Earnings Call

Company Participants

- Lincon Lopes Ferraz, Chief Financial Officer and Investor Relations Officer

Presentation

Operator

Good afternoon, ladies and gentlemen. At this time, we would like to welcome everyone to the Positivo Tecnologia's Fourth Quarter 2017 Earnings Conference Call. Today we have with us Lincon Ferraz, Investor Relations Officer.

We would like to inform you that you are in listen-only mode during the company's presentation. After Positivo Tecnologia's remarks are completed, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions) We have simultaneous webcast that may be accessed through the company's website at ir.positivotecnologia.com.br in the MCIQ platform. The slide presentation may be downloaded from this website. Please feel free to flip through the slides during the conference call.

Before proceeding, let me mention that forward-looking statements are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Forward-Looking statements are based on the beliefs and assumptions of Positivo Tecnologia's management and on information currently available to the company. They involve risks, uncertainties and assumptions, because they relate to future events and therefore depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of Positivo Tecnologia and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the call over to Mr. Lincon Ferraz, Positivo Tecnologia's Investor Relations Officer. Mr. Lincon, you may begin your conference.

Lincon Lopes Ferraz {BIO 18660463 <GO>}

Good afternoon. We are here to present the results of the fourth quarter 2017 when we posted operating cash flow of BRL121 million. The period was marked by the increase of 71% in sales of PCs in Brazil in the last quarter, of which 18% growth in retail, 345% in government and 65% in corporate segment. This resulted in an increase in market share of PCs in Brazil by 5 percentage points, reaching 18%.

In the mobile phone market, we had a highly competitive environment, which continues, so the sales in the market concentrated in the three largest manufacturers.

Net revenue in the last quarter was BRL587 million, 50% up; and BRL1.9 billion in the year 2017, 10% increase over 2016. Adjusted EBITDA reached BRL23 million in the quarter and BRL123 million in the year, representing a margin of 6.4%.

Adjusted net income totaled BRL4 million in the year, and we have a strong drop in net debt to 140 million, which is a 33% reduction, with net debt over adjusted EBITDA of only 1.1 times. There is a subsequent event, which is a sponsorship agreement with Corinthians soccer teams for the 2018 season.

Well, let's move to page four to see some of the computer segment context. So we saw recovery in the year following the improvement of consumption indicators in Brazil. PC market grew 21% in Brazil in the fourth quarter. December was the 13th consecutive month of steady growth of the Brazilian market year-over-year. The retail segment increased by 28% and government doubled the volume year-over-year.

It's important to state that January 2018 grew by 37% over January 2017, so the market is growing very fast right now, the PC market is growing very fast following the crisis between 2014 and 2016, when the Brazilian PC market reduced by 67%, which was our massive reduction.

On the right side of the chart, we can see the company actions. So we made a lot of efforts to capture this momentum. Our sales in Brazil grew by 71% in the quarter. In the retail, we had an immediate blockbuster, which is a ultra-thin notebook priced at under BRL1,000 very competitive price. And in the government, we made all the arrangements to perform one of the largest revenues of the company's history in the segment, which totaled 255 million. And in the graph below, you can see the trend for our market share, representing 17.8% in the fourth quarter. On average, in the year, it was 15.3%.

Moving to page 5, speaking about mobile phone. So the price war continued among the leading brands in the fourth quarter. This limited the space for the other competitors. You can see that the top three brands, which are Samsung, LG and Motorola, they have 80% of the market, and letting only 20% for other brands such as Positivo, Apple, Alcatel and other names. So it was very tough for the small manufacturers, and our market share reduced to 3% only in the fourth quarter coming from 4.8% in the same period 2016.

We present some charts below where you can see the prices of the top-selling smartphones in Brazil. So here we have the top-selling smartphones from Samsung, Motorola and LG. You can see the trend. They reduced a lot the price with a slightly increase in some case in December, but if you compare with the price bracket [ph] in March, there is a significant reduction.

Moving to page 6, here we have some color on the sponsorship agreement with Corinthians. Corinthians has one of the largest fan base in the world, they have 30 million fans. We have a contract until October 2018, and we have an extension option to December 2018. We expect a strong increase of the brand's exposure on primetime TV and top tier media channels.

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Moving to page 7. Here we have some highlights and outlook for the company. In the retail of PCs, the margins have been healthy and the sales volumes have been in line with our internal projections, this is helping a lot to keep inventories optimized. We expect an increase in demand for 2018. As I mentioned, the markets began 2018 with a strong growth of 37% in January. In February, we just received the data, it is 19%.

For computers in the government segment, we have contracted portfolio for delivery in 2018, that already exceeds the revenue recognized in 2017. So we can have a very important growth of revenue in this segment in 2018. Just to mention that, this year we have elections in Brazil in October. So this may concentrate some revenue in the first nine months.

Mobile phones, the unfavorable competitive environment is expected to continue in the first quarter. We see some improvements for the second half of the year, but right now, there is -- the market is still tough and we are moving some volumes to Argentina and Chile in the first half, looking to sustain our volumes and all the benefits that we have when we can keep volumes in this segment.

Regarding cash generation, this year as I mentioned, we have more revenues, both in retail and government. And in the case of government, a concentration due to the election period. So we expect an increase in working capital in the first and second quarters. This should increase a little bit our net debt, but it will normalize at the end of the year.

Our joint venture with Hi Technologies, the start-up company that we purchased I think in 2016, is going fine. Right now, this company is in advanced discussions with investors for a new round of fundraising. So this the moment for them to expand the operation. And the operation of Hilab service is very, very cash demanding, so with the help of investor, we should go through this process movement [ph].

In the digital TV project, we have BRL70 million contracted for delivery in the first half. And right now, there is a new bidding process in place. We were informed that we are very well positioned, so we should increase this BRL70 million contracted to maybe BRL150 million for delivery in the year.

Moving to page 9, talking about the financial results. First of all, we have a recognition of non-recurring expenses in the fourth quarter, mostly with no cash effect. The first one was a provision for obsolete inventories. It was necessary due to a delivery refusal that we had by one client from the government segment. We believe that the likelihood of realizing this asset at cost will be low. So we decided to make this provision. We are doing some efforts to deliver this product to other clients, and if we succeed, this could result in a reversal of part of this provision.

The second one is the Fiscal Installments Program. In Brazil, in the second half 2017, the Brazilian government promoted installment tax program in order to generate cash for the National Treasury, and we jointly [ph] Positivo made its adhesion to just PERT [ph]

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program. It resulted in a recognition of BRL23 million loss in the income statement, but only 7 million was really cash.

And the last one is the expenses, our debt expense that we have in our factory closure in Argentina. We mentioned about this in the release of the first quarter results 2017 and the migration of motherboard production from Curitiba to Manaus. So this is the last step of the Manaus project, it costed [ph] some agreements with employees. We had also the ramp-up production in the new factory, it costed us BRL3 million.

Moving to page 10, here we have the volumes of the period. As I mentioned, in all the segments, we grew in the PC segment, 12% in retail, 33% in government, 65% in corporate. Sales were strong in Brazil, 71%, and reduced in abroad in the joint venture Positivo BGH, because of, in the fourth quarter 2016, we had big delivery in Kenya and Africa that we didn't have in the fourth quarter 2017. Mobile phones reduced 37% in the smartphone category and grew by 23% in the feature phone category.

Moving to the next page 11, here we have the revenue figures. Net revenue totaled BRL587 million, it's 50% up year-on-year, and in the year 2017, the growth was 10%. You can see the price trends, we have an upward movement in Desktops, mainly because of the concentration of government projects in the fourth quarter. Government products are priced, they are better configured, they have more term of guarantee, so they have three years, even five years of technical assistance. So this is priced, so that's why the price increased so much.

Moving to page 12, we have the variable costs, cost of goods sold and also the selling expense. Cost of goods sold increased to 77%. This is a combination of the increase in the prices of memory cards in dollar terms. The second one is the increased proportion of national component that we are obliged to purchase due to local regulations and these components are much more expensive, when compared to the components that we import.

And also the high proportion of government sales make the COGS [ph] represent more in terms of revenue, but it's compensated in the selling expense. As you can see in the chart in the right side, selling expenses reduced a lot year-over-year, because sales to the government does not have provisions for marketing. So marketing expenses came from 10% in the fourth quarter 2016 to only 5% in the fourth quarter 2017.

G&A expenses were almost flat year-on-year. We are doing a very strong control here and we expect to keep this base in 2018.

Page 13, here we have the results. Adjusted EBITDA in the year was 123 million; this implies multiple net debt over EBITDA of only 1 time. Adjusted net income in the year was 4 million, was a positive 4 million, but if you consider the actual net loss, it was a loss of BRL47 million in the year because of those non-recurring events that I explained.

Moving to page 14, working capital and debt. The working capital reduced a lot in the fourth quarter. This was due to the sales to the government. They were postponed from

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the second and third quarters of 2017, so in the fourth quarter, there was a rush to deliver all the projects. And both Positivo and the clients, made a lot of efforts to guarantee these deliveries because the disbursement, we were committed for disbursement in the year. So, there were some changes where we receivables -- we collected the receivables, but the supplier was still open. So we saw a big cash regeneration here.

Net debt closed at 140 million. This is the lowest level since 2012. And another movement that helped us generating cash was the monetization of tax credits of BRL40 million, helped by the digital TV project.

We closed the year with a cash position of BRL388 [ph] million, very strong cash position that make us comfortable to meet the capital requirements for this growth in 2018.

That's it. Thank you very much.

Questions And Answers

Operator

Thank you. The floor is now open for questions. (Operator Instructions) This conference has now ended. Thank you for attending today's call. You may now disconnect your lines.

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