

Y 2016 Earnings Call

Company Participants

- Lincon Ferraz, Investor Relations Officer

Presentation

Operator

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to Positivo Informatica's Fourth Quarter 2016 Earnings Conference Call. Today we have with us Lincon Ferraz, Investor Relations Officer.

We would like to inform you that you will be in listen-only mode during the company's presentation. After Positivo Informatica'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 www.positivoinformatica.com.br/ir and Engage-X 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 Informatica'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 Informatica 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 Informatica's Investor Relations Officer. Mr. Lincon, you may begin your conference.

Lincon Ferraz {BIO 18660463 <GO>}

Thanks. Good morning, everyone. We are here to present the results for the fourth quarter 2016, when Positivo Informatica recorded net income of BRL8 million, it was recorded from the net loss of BRL80 million in 2015. While [ph] the company posted recovery of profitability, even with the Brazilian economy in deep recession and highly unfavorable consumption environment. We maintained its market share in the PC market,

reaching 15%. We had a continuous progress in the diversification of the business, with mobile phones reaching 39% of consolidated net revenue in the fourth quarter. It was 126% growth year-on-year in terms of net revenue. And our market share reached 4.8%, it was up by 2.5 percentage points.

We have further reduction in recurring general and administrative expenses of 29% in quarter -- fourth quarter 2016 compared to the same period of last year.

Our adjusted EBITDA reached BRL36 million, it was three times more than the same period last year. And as I mentioned, net income reached BRL9 million in 2016.

As I'm going to present to you, we have a good evolution of cash generation projects, with a reduction in excess inventory and also monetization of tax credits.

Our net debt reduced to BRL220 million, it is the lowest level in five years, and our ratio of net debt EBITDA reached only 1.5 times.

In this period, we began to expand in Africa in the fourth quarter, we started to deliver new educational project in Kenya. This delivery is going to happen throughout the first half of 2017.

So, let's move to the page number four. Key results about the market scenario and the company actions. The PC market fell by a 11% in the fourth quarter and 32% in the year. So, the economy crisis in Brazil had a big impact in the PC market. In the retail, the reduction was 19% in the fourth quarter, 29% in 2016. The fact is, the reduction was in line with industry expectation. The unemployment rate is driving this reduction, it reached 12% in Brazil in December 2016, it's the highest level since 2012. We have especially unfavorable dynamics for the items of higher ticket price in the retail, because it is sold in installments. So when the credit goes down, this kind of product have a higher reaction when compared to the products that are low ticket price.

In the government in Brazil, they have in 2016 a big political instability and a lot of measure for cost control. So the volume of bid reduced dramatically throughout the year. The good news is there is an expectation for our recovery in 2017, we can see in the first months of 2017 that develop of bids is much higher when compared to the same period last year.

Mobile phones have better dynamics, it grew by 15% in the fourth quarter; in the year it was a small reduction because of the crisis. The category is less affected, because it's considered a first necessity by the consumers. This can be proved by the survey led by Google and Ibope in the Black Friday 2016, when smartphones let the electronics category by 38% share of consumer purchasing intentions.

The company actions mainly in terms of diversification, we had a big revenue for mobile phones, it will again, triple digit reached 38% of consolidated net revenue, it was BRL150 million. The Quantum brands are new brand for mobile phones accounted for 43% of consolidated mobile net revenue, it was a growth of 400% or I mean five times more

when compared to the fourth quarter 2016. As you can see, we have a strong evolution of profitability and cash generation.

Moving to page five, we can see the figures. In the left, of market share, Positivo's market share in the mobile phone in Brazil.

In 2015, we began with below 1% market share and we closed 2016 almost in 5%, so this growth is driving the revenue increase of mobile phones and is very important because mobile phones in Brazil, as you can see in the right side of this page, is four times bigger than the PC market in Brazil, it's \$13 billion market and PCs is \$3 billion market and our market share is only a small portion when compared to our share in the PC market in Brazil.

Moving to page six. Here you can have more color on the results of -- in terms of profitability and cash. Beginning with the margins; in the fourth quarter 2016, we reached 14%, it was a big increase year-on-year. We have projects [ph] of after sales efficiency, manufacturing efficiency, logistics and so on. This is helping a lot to increase our contribution margin.

In the fixed costs, as you can see in the left side below, we have a strong reduction, 29% in the fourth quarter 2016 when compared to the same period of 2016. We had a downsizing the administrative structure of the company in April 2016 that led to this reduction.

In terms of cash, we have two projects, the first one is the recoverable taxes, we expect it to monetize BRL80 million in 2016. And we -- actually we had a better performance than expected and reached BRL88 million, so you will see in the next page that this helps a lot to reduce net debt in the year.

Excess inventory, we closed 2016 with BRL135 million of excess inventory and this year we closed only BRL62 million as a reduction of BRL73 million. This is the inventory for which we don't have a clear forecast of sales, so that's why we call it excess inventory. It's very important for us to keep this low, so this helps a lot also to protect the margins.

On page seven, we can see company outlook for 2017. The most important thing is the mobile phone segment. We expect to grow although at a less intense level when compared to 2016, because of their comparison basis is much higher. We rely on the Quantum brand to drive this growth, because we introduced Quantum in the retail channel in the second half of 2016 and we expect this to be matured throughout 2017. Also we have special projects for payment terminals that we have a partnership with CL [ph] and this can bring to us extra revenue for mobile phones.

The second thing is the Digital TV Project. In Brazil, they are switching off the analog signal for TVs in favor of the digital sign [ph] and we are participating in a bid to provide digital convergence for 14 million families of the Bolsa Familia program.

So we own part of this bid, already have a contract signed of BRL270 million to be recognized between February and September 2017. Right now, we have some bids happening and we expect to increase this amount already contracted in both revenue from these projects in 2017.

The third thing is our expansion in Africa. We have a new project in Kenya, this is a total volume of over 300,000 devices, most of the devices are tablets for students. This is a contract signed through our joint venture with BGH Group in Argentina. So this contract have a revenue for this joint venture of \$100 million between December 2016 and the first half of 2017.

The fourth thing is VAIO launch in South America. In September 2016, we started to sell VAIO brands in Argentina. We also licensed this brand to Chile and Uruguay, we began selling in Chile in February 2017, and we expect to register to recognize the first sale to Uruguay in the second quarter of 2017. Also this operation is managed by our joint venture with the BGH Group in Argentina.

And the fifth project is the launch of medical technology products. We acquired 50% of its capital of Hi Technologies (inaudible) company. They are in the healthcare business. We have important launch to be -- to be disclosed in the first half of this year, and we expect this product to be a blockbuster. Let's see what happens in this launch.

Moving to page nine, looking to the financial results. The first thing is that our revenue from our sales of mobile phones went up by 140%, a very strong growth. 120% for Positivo brand and 500% for Quantum brand.

When I take a look at the feature phone business, we reduced by 33%, but actually this market is shrinking worldwide and we are not focusing this because we don't have a long-term perspective, so we are focused more in the smartphone segment.

PC sales, you can see a reduction in the three segments. In retail and corporate reflects the crisis in Brazil, the demand is very weak. In the government, specifically, is a big reduction. This is our consolidated sales, so we have Brazil, Argentina, Africa and so on.

If you take a look at the government and consider only Brazil, the reduction will be 80%, so it's a massive reduction. As I mentioned it, we expect to recover this in 2017, because of the volume of the bids are increasing a lot in the beginning of 2017.

Moving to page 10. Now, in terms of net revenue, net revenue in the year was down by 5%, mainly because of the computers, and in the fourth quarter by 21%, we have issued with recognize of revenue. In the government segment, we had accounting cut-off of BRL100 million, which is three times more than the usual. So, excluding this effect, the reduction would be a single digit like 9% -- 8%, 9%.

As I mentioned, 38% of revenue was mobile phones and in the year 31% represented by mobile phones. As you can see in the graph below in the retail, actually we grew 13.2%

[ph] and the big reduction is in the government segment with 65%, it's a massive reduction. So that's what led the reduction in the consolidated net revenue.

Moving to page 11, here we can see cost and also expenses. In the cost side, we have a big improvement year-on-year, it's a 15 percentage points reduction in terms of cost of goods sold. This is because in the first part of 2015, we had a very intense sell of inventories. At that period, we were very high in terms of inventory levels, so we had to put some effort in the sales, we give discounts and everything to push sales. In 2016, almost -- after the second quarter of 2016, we didn't have to give discounts to promote sales, so that's why the gross margin is recovering so fast.

When you compare the third quarter to the fourth quarter, there is a slight improvement, but this is offset by the increase in the selling expenses because of the increase in the marketing line, as you can see, it reached almost 10%. It's because most of sales in the fourth quarter were to retail segment where there is a lot of commercial expenses related to the sales.

In the G&A expenses, here you can see the big reduction that our projects to restructure the administrative structure of the company, you can see year-on-year 29% reduction and when you compare quarter-on-quarter, third quarter 2016 with the fourth quarter, a slight increment of 3.8% (sic). This is because of the bargaining agreement we had in September an extra bargaining agreement of 2%.

Moving to page 12, we can see the results. In terms of EBITDA and also net income, adjusted EBITDA reached BRL36 million, this is three times more when compared year-on-year. It is slightly above when you compared to the third quarter 2016, this is because of the contribution margin which is better right now. This recovery led to the reversal of the net loss that we recorded both in the fourth quarter 2016 and the fiscal year 2016 -- 2015. So we now have BRL1 million of net income in the fourth quarter and BRL9 million of net income in the year. The financial result was a net expense of 25 million, in the exchange rate variation we lost BRL9 million, half of this loss is related to the Digital TV program that we are going to deliver in 2017. So, at least half of this loss we can recover in 2017, when we recognize the revenue from this project.

Moving to page 13, here we try to consolidate the net income with the change in net debt, you can see that recoverable tax project was a success. It helped a lot. We lost part of this in the working capital. So the cash generation before investment reached BRL80 million. Investments totaled BRL37 million, we invested a little bit more in 2017 -- '16 because of the change of production of mobile phones from Curitiba to Manaus, so we have to prepare the factory for that. But even with this impact we had a BRL44 million reduction in net debt.

Moving to page 14, we can see that net debt reached BRL220 million, the lowest close that we had in the best five years in terms of net debt and the ratio between net debt and EBITDA reached 1.5 times, which is very healthy.

In the last page, page 15, we can see some figures of in the capital market, our share price is rising. We closed 2016 with 2.79 and in the end of February it was higher than 4. So the daily trades and average daily volume in terms of financial volume is increasing a lot as you can see in the graphs. So we are very excited about that. We expect to keep gaining price and deliver our best -- better results for our shareholders.

So, I'll finish my part here. Thank you very much for your attention. See you in the next quarter.

Questions And Answers

Operator

Thank you. The floor is now open for questions. (Operator Instructions) There appear to be no questions at this time. The conference have now concluded or the question-and-answer session have now concluded. I'll turn it over to Positivo Informatica for final considerations.

A - Lincon Ferraz {BIO 18660463 <GO>}

I would like to thank you all for your attention and see you in the next conference call. Thank you. Bye-bye.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect the lines.

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