

## Q3 2014 Earnings Call

### Company Participants

- Clovis Poggetti, CFO & Director-Investor Relations
- Rômulo de Mello Dias, Chief Executive Officer

### Other Participants

- Alexandre Spada, Analyst
- Carlos Macedo, Analyst
- Jorge Kuri, Analyst
- Mario Pierry, Analyst
- Tito LaBarta, Analyst

## MANAGEMENT DISCUSSION SECTION

### Operator

Good morning, everyone, and thank you for waiting. Welcome to Cielo's Third Quarter 2014 Results Conference Call. This event is being recorded and all participants will be in a listen-only mode during the company's presentation. After Cielo's remarks, there will be a question-and-answer session. At that time, further instructions will be given.

This event is also being broadcast live via webcast and may be accessed through Cielo's website at [www.cielo.com.br/ir](http://www.cielo.com.br/ir) where the presentation is also available. Participants may view the slides in any order they wish. The replay will be available shortly after the event is concluded. Those following the presentation via the webcast may post their questions on our website.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of Cielo's management and on information currently available to the company. They involve risks and uncertainties because they relate to future events and therefore depend on circumstances that may or may not occur. Investors and analysts should understand that macroeconomic conditions, industry conditions, and other factors could also cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Rômulo de Mello Dias. Mr. Romulo, you may begin your presentation.

### Rômulo de Mello Dias

FINAL

Bloomberg Transcript

Good morning. I'd like to thank you all for joining us as we present our results from the third quarter of 2014. With me today are Clovis Poggetti, CFO and Investor Relations Officer and several members of the management team, finance, and IR teams.

On page three we can see the highlights of the quarter compared to the same period last year. In Q3, Cielo's net income totaled R\$817 million, up 18.5% year-on-year. EBITDA reached R\$957 million, up 3% and EBITDA margin at 49.4%. Transaction financial volume totaled around R\$129 billion, up almost 14%. Net operating revenue reached 1.9% (sic) [R\$1.9 billion] (2:39), up 11.6% year on year.

Now let's present the awards received during the quarter. By the fourth consecutive time, Cielo reached first place in the Financial Services category in the Melhores da Dinheiro ranking from IstoÉ Dinheiro magazine; that's from IstoÉ Dinheiro magazine. By the seventh time, Cielo reached first place in the Specialized Services category in the Valor 1000 ranking from the Valor Econômico newspaper.

Cielo was selected Company of the Year and first place the third consecutive time in the Financial Service category of the yearbook from Época 360°, Época Negócios magazine. The 17th most valuable brand in the Brandz Ranking prepared by Millward Brown in a partnership with WPP. Also considered the Best Company of the Year in the 2014 Institutional Investor magazine, Best Team of Executives, both by the buy side and the sell side. Cielo was placed among the best companies to work for the first place in the Banking and Financial Services category from Você SA magazine. And finally, the Financial Service company that generates most value in the More Value Generated ranking from the Consumidor Moderno magazine.

On the next slide, number four, we have the evolution of our transaction financial volume with credit and debit cards. Looking at the breakdown by products, we can see that the credit volume was up 11% and the debit volume 18.3% over Q3. The total debit amount, without considering the Agro product, a product that has a specific characteristic with a very low price due to extremely high tickets, debit volume would have increased 16.8%.

Regarding the immediately previous quarter, credit volume increased 3.4% to R\$78.6 billion, while debit was up R\$1.75 billion to R\$50.2 billion. Again, without considering Agro products, debit volume would have increased 5.3% over Q2.

On page five we present graphs with the financial volume and the growth rate evolution per quarter for the years 2012, 2013, and 2014. As already mentioned in the previous quarters, we have a statistical challenge ahead of us. As a matter of fact growth rates this year should follow the same trend from 2012 but with lower values.

On page six, we present a number of transactions captured in Q3. There is a growth of 13% in Q3 compared to the same period of 2013, representing an amount of 1.4 billion transactions. Compared with Q2 the number of transactions increased by 4.1%.

On page seven, we have our operating indicators. We present a number of active points of sales which has record one transaction in the last 30 days and the number of installed

POS. We can see in the graphs that all indicators show growth in the periods. In comparison to the first quarter of 2013 the basis of installed POS grew 10.5% in comparison with the previous quarter, increased by 1.9%. Wireless terminals reached 61% in Q3. The increase of the active points of sales reached 12.5% compared to the same period last year. In comparison with Q2 there was a growth of 4.6%.

Now I'd like you to hand the call to Clovis Poggetti who will continue our presentation.

### **Clovis Poggetti** {BIO 16529642 <GO>}

Thank you, Rômulo, and good morning, everyone. On page eight, we have our net operating revenue, which totaled R\$1.9 billion, growing 11.6% over third quarter last year. The increase in net revenue is chiefly related to the ongoing business expansion and an increase in revenue generated by the subsidiary Merchant e-Solutions, the latter impacted by the dollar appreciation. Compared with the second quarter of 2014, net operating revenue presented a growth of 5.3%.

On the next page, page nine, we have our expenses. The expenses reached at R\$1.1 billion in the third quarter of 2014, up 20% over the same quarter of 2013 and up 10% over the second quarter this year. The cost of services provided was R\$781 million in the quarter, growing 19.3% and 11% year-on-year and quarter-on-quarter respectively.

Preparing the items (8:04) that most impacted cost in the period, we have mainly increased costs related to transaction such as capturing and processing transactions, call center, fees paid to the brands and telecommunications given the increase in the transaction volume. Increased costs related to subsidiary Merchant e-Solutions due to the appreciation of the dollar, the M4U and also increased costs with projects. Quarter-on-quarter, the rising cost is related to higher expenses with subsidiary Merchant e-Solutions, which are impacted by the appreciation of the dollar and M4U and equipment maintenance and net activation costs due to the exchange discontinued equipment for new ones and increasing wireless technology equipment and also increased costs with projects.

Our operating expenses represented R\$306.6 million in the third quarter this year, up 22.6% compared to third quarter last year and 7.5% compared to the second quarter this year. The increase in expenses over the same period last year is mainly related to the personnel line mainly due to the increase in the head count of the project teams, especially IT and operations, and the increase in salaries agreed with the union and also to the sales and marketing expenses line. This variation is mainly due to higher sales and partnership campaigns, institutional media purchases in the third quarter this year, partially offset by a reduction in other net operating expenses.

In the quarter-on-quarter comparison, the increase was chiefly the result of the increase on sales and marketing expenses due to higher volume of sales and marketing initiatives in the third quarter this year compared to the previous quarter and due to increase in the head count of the project team, especially IT and operations, and the increase in salaries

agreed with the union as mentioned earlier, partially offset by the reduction in general and administrative expenses.

On the same slide, we can see total expenses per transaction at R\$0.77, up 6.4% compared to the third quarter last year and 5.7% higher than the second quarter this year. The additional amount in the quarter was simply due to projects. The most relevant being BOB, Best of Both, which is the adaptation of the U.S. company platform for use in the Brazilian market, expected to last until mid-2017 and the customer service project that in the next year should stop putting pressure in the company's expenses. Thereby it should be expected that our spending per transaction next year to be lower than the range achieved this year.

Financial results, which we can see on page 10, are mainly results from prepayment of receivable operations. It's worth mentioning that starting this quarter the prepayments of receivables results will be presented and the variation with respect to the previous quarter lies in the fact that in addition to adjustment to the present value, the interest on prepayments of receivables with issuers is also considered.

I want to take this moment to highlight a change made in the presentation of our balance sheet. From this quarter on, it will be highlighted the balance of our prepayment with the issuing banks. This information was already available in the explanatory notes, but we prefer to give the highlights to facilitate the analysis of the company's leverage. As you can see by reading the balance sheet, the prepayment balance with the issuers was R\$3.4 billion in the third quarter which should be considered as debt.

Now going back to our prepayment of receivables business, in the third quarter of the year, result was R\$404.7 million, an increase of 66% compared to the same period of last year and 15% in relation to second quarter this year.

As usual, let's also present the result of the managerial analysis of net cost of funding. In this analysis, every resource used to prepay receivables is applied the same cost of funding we have when we prepay our receivable flows with the issuer banks. According to this managerial analysis, net revenue was R\$240 million for the quarter, increase of 63.5% and 10% compared to the third quarter last year and second quarter this year, respectively.

Additional indicators regarding the prepayment of receivable operations are shown on slide 11 where we can see that prepaid volumes shows an increase of 18.6% year-on-year and 2.2% quarter-on-quarter. The amount in the quarter totaled R\$13.9 billion, or 17.7% of total credit volume. Starting this quarter, the prepaid volume breakdown between credit installment and regular credit will also be presented. And for the third quarter this year the breakdown stood at 64.6% for the credit installment and 35.4% for the credit regular credit.

On slide 12 we have our financial performance with EBITDA in both absolute amounts and margins. EBITDA totaled R\$957.3 million in the third quarter this year, 2.9% year-on-year. EBITDA margin was at 49.4% in the third quarter. EBITDA margin was down by 4.1

percentage points over third quarter last year. Compared to the second quarter, EBITDA increased by 0.2% and margins decreased by 2.5 percentage points.

On slide 13, we show that our net income total R\$817.4 million, up 18.5% year-on-year with a net income margin of 42.2%. Finally, when compared to the second quarter this year, net income presented increase of 2.6%, while margins dropped 1.1 percentage points. Now, I'll go back to Rômulo.

## Rômulo de Mello Dias

Final considerations refer to the macroeconomic scenario. I think no one doubts that we'll have a very challenging year in 2015, and despite we still believe an increased penetration of the card as means of payments, attendance that continues to happen, we may eventually suffer some consequence of a slowdown in the sharp consumption.

On the positive side, you may recall that we are tentative in the short term by an increasing inflation, as long as it does not impact consumption. That is what I want to share with you and thank you for your attention.

Now we are ready to take your questions. Operator, please?

## Q&A

### Operator

Ladies and gentlemen, we will now begin the question and answer session. Our first question comes from Mr. Carlos Macedo with Goldman Sachs.

### Q - Carlos Macedo {BIO 15158925 <GO>}

Good morning. Thank you for taking my questions, Rômulo, Clovis. I have a couple. First, if you could just give us a very brief update on how the regulation negotiations around the regulation for the final exclusivities are going, if you have any? And then I have a follow-up there.

The second one would be on the cost side, the cost plus expenses for transaction at R\$0.77, we're talking about going down to R\$0.73 potentially next year. Just a question regarding what kind of impact - if you're still holding that kind of objective? And second, what kind of impact would a much weaker real or a stronger dollar have on that absolute number, given the expenses that come out of Merchant e-Solutions? Thanks.

### A - Rômulo de Mello Dias

Thank you, Macedo, for your questions. I will answer the first one and the second Clovis you take care. Regarding regulation, and the end of prefer agreements that you have some brands (17:08) with some networks and as well our competitors have the same. I

would say that by the beginning of next year, we should be ready to capture - all of the acquirers to capture all the networks on the branch.

**Q - Carlos Macedo** {BIO 15158925 <GO>}

And a question, Rômulo, if I may, just on the discussion between doing it as a value-added network or as an acquirer, has that evolved in some way that you can share?

**A - Rômulo de Mello Dias**

Not very much.

**Q - Carlos Macedo** {BIO 15158925 <GO>}

Okay. And so just a final question on that. If you were to capture, for instance, volumes in American Express that if I'm not mistaken today are volumes that you capture as a value-added network, if that were to be converted into an acquiring revenue for you, it would increase your volumes that you report and also your revenues by the value of the American Express network. Would that be correct, without a major impact on cost?

**A - Rômulo de Mello Dias**

If it were the case, correct. But I wouldn't expect, let's say, a high probability in the case of AMEX to have this kind of scheme. In the case of ALO (18:21), if it becomes a network, if it becomes a (18:24) service, of course, our volume would be decreased because we wouldn't capture the volume. We would be just a service provider with some additional service that we will continue to provide to ALO (18:39).

**Q - Carlos Macedo** {BIO 15158925 <GO>}

Is there any way that you can size the potential impact there if that were the case?

**A - Rômulo de Mello Dias**

At this stage, I think not. What we can tell you that ALO (18:51) is becoming more and more important and we made strong investments since Cielo (18:57) was launched some three years ago, and the same thing happened in the case of the LOC (19:03) in the banks distributing the cards to their customers. And what we did in the last year was the most important year of course for ALO (19:16) and for us - sorry, this year was the most important year for ALO (19:21) because of the investment that we did so far. And now ALO (19:24) has a very good acceptance around Brazil from the north to the south.

**Q - Carlos Macedo** {BIO 15158925 <GO>}

Okay. Thank you on that. So on expenses.

**A - Clovis Poggetti** {BIO 16529642 <GO>}

Hi, Carlos. I will take advantage of your question, if you please allow me to give one step back, and let's recall what we already mentioned in previous quarters regarding this issue, okay.

FINAL

So first, we did already expect an increase in our total expenditure, okay, which means cost plus expenses per transaction, and these two to higher expenses with projects. Okay? We have the BOB project that you are already aware of, which means the totalization (20:08) of the Merchant e-Solutions platform, and this one in terms of investments, we believe, we will let until 2016, mainly beginning 2017.

We also have projects related to customer services, projects that we believe will strongly contribute to our leadership position, and regarding these ones, the expenses and investments will be taking place this year mainly and part of next one. My point is that once these projects are delivered, so next year the customer service ones (20:48) in 2016, 2017 for BOB, total expenditure should go back to regular levels.

For this year what we said is something between R\$0.75 and R\$0.78, and please consider the bottom, the floor of this range, and for next year what we said is it is fair to assume a range lower than the one we present this year.

**Q - Carlos Macedo** {BIO 15158925 <GO>}

Fair enough, Clovis. And that's what I meant when I said R\$0.73 is lower than the range, though it might not be quite as low as that. Now if you do get a weakening of the real, would that affect your expected range?

**A - Clovis Poggetti** {BIO 16529642 <GO>}

No, no, no. Let's say that Merchant e-Solutions, despite the fact that the interchange is considered a cost for Merchant e-Solutions, it is accounted as a cost, the total cost of Merchant e-Solutions is not relevant, let's say, compared to the overall cost and expenses, let's say, taking the consolidated company.

**A - Rômulo de Mello Dias**

And also on the other hand, the revenue would be -- if something happens in this regards, it would be good for the revenues because we charge in dollar.

And another point that we should make that we - maybe the effect that we could have is related to CapEx, and by CapEx I mean when we buy POS because there is a correlation between the price of the POS and the dollar, some kind of correlation.

**Q - Carlos Macedo** {BIO 15158925 <GO>}

Okay. Thank you for the...

**A - Rômulo de Mello Dias**

But it's not something that would make, let's say, a strong difference in our numbers.

**Q - Carlos Macedo** {BIO 15158925 <GO>}

Perfect. Thank you for the complete answers.

## Operator

Our next question comes from Tito LaBarta with Deutsche Bank.

### Q - Tito LaBarta {BIO 20837559 <GO>}

Hi, good morning. Thanks for the call. A couple questions, just first in terms of volume growth, you had mentioned we are seeing a little bit of a slowdown. But just wanted to get your thoughts going into 2015, particularly with a continuation of the current government and expected relatively weak economy, just how do you think volumes will go into next year? If you could maybe give a little color on that.

And then my second question, there was some noise recently about the potential regulation of the prepayment business. If you can maybe just give some color on that and if you do expect to see any regulation there? Thank you.

### A - Rômulo de Mello Dias

Thank you, Tito, for your questions. Regarding the volume growth, we said that we were expecting for this year between 16% and 18%, and now we're, let's say, better forecast considering information that we have in our hands, now it's more close to 16% for the industry, not for Cielo. And we also said that for this year Cielo would grow below the growth of the industry.

For the next year, I would say that maybe it's too early to say something, but again, with the information that you have, I would say that probably the industry will not grow on the same speed, with the same speed that they present this year, probably a little bit lower. And the second question, you had mentioned about regulation of prepayments, I don't know if you mean maybe to change the type of payments, is what you're saying?

### Q - Tito LaBarta {BIO 20837559 <GO>}

Yes, there was some news about - some talks about that recently (24:44).

### A - Rômulo de Mello Dias

Okay, not regulation of prepayments, but maybe to - the credit in 30-days debate.

### Q - Tito LaBarta {BIO 20837559 <GO>}

Exactly.

Okay. I mentioned that in let's say Cielo Day that we need to consider many things in order to have, let's say, a bad opinion. Let's try to make a comparison between American model and Brazilian model.

In American model, American system, if the customers don't pay their bill on the 30-day, the interest rates, they go back until the date of the purchase. And they have in U.S., depends on the bank, around 30% to 40% of people use the revolving line, which means



that they are paying for the ones that pay their bills without delaying, without postponing. And also the interest rate in the case of U.S. is 0.25%. Today just a curiosity, Sweden reduced the interest rate from 0.25% to 0%. So what you're saying that the interest rates maybe even if they go up, let's say, after a certain period of time, they are very low and the cost of this is almost nothing when you talk about 30 days.

In the case of Brazil, SELIC as you know is 11%, so almost 1% per month, which means – in other words, it makes a lot of difference when compared to the cost upward (26:28) to have the negative floating is really high.

Also, another option that could, let's say, happen, let's imagine a hypothetical situation, when the customer wouldn't have anymore, let's say, the floating, because as you know, the industry don't take advantage of the floating. Who has, let's say, a certain period of time to pay their dues? The customers. And the customers when they have a certain period to buy, if this period is reduced to two days, for instance, what would happen in terms of consumption? The consumption, for sure would suffer. And even if international model, even if the American model would be applied here to Brazil, I would say that the consumption would suffer because at the end of the day there's no free lunch.

Thanks. That's very helpful. So from your point of view, you think the chances of changing the regulation there are small, or relatively (27:38)?

## A - Rômulo de Mello Dias

I wouldn't say that because I cannot talk by the regulators, but I'm just trying to provide you with some figures in order to allow you to have, let's say, to make your judgment about impacts. It's different. Another information, here in Brazil 15% of the cardholders, they use a revolving line, okay. So it's much lower of course because it's much more expensive.

When you have 30%, 40% using the revolving line and the interest rate being applied since the date of the purchase with a 0.25% interest rate per year, it's completely different, let's say, to the system could afford much more when there are some differences such as the ones that I mentioned to you.

## Q - Tito LaBarta {BIO 20837559 <GO>}

That's very helpful. Thank you very much.

## Operator

Our next question comes from Mario Pierry with Merrill Lynch.

## Q - Mario Pierry {BIO 1505554 <GO>}

Hi, Rômulo. Thanks for taking my questions. Again, I asked most of my questions during the Portuguese call, but let me ask you two additional questions, primarily related to the prepayment business.

FINAL

One is we have seen right you're charging much higher rate on prepayments, but at the same time your funding costs have not risen as much. So just wanted to understand from you, why are you able to keep your funding costs lower? Is it because you are using more of your own capital or what is the trend there? Should we eventually expect funding costs to rise for you as well?

And then second question is more looking over the medium- to long-term, right, when we break down your business between the acquiring business and the prepayment business, we see that the acquiring business, just judging by the EBITDA, is growing low single-digits, while your prepayments is growing more than 60%. So in the future, in the medium-term, do you expect to have like roughly - what is the proper revenue mix that we should think about? Is it like a 40% contribution from prepayment or is it 20%? What is the numbers that you would feel comfortable with?

### A - Rômulo de Mello Dias

Mario, thank you for your questions. Regarding prepayments, yes, we charge higher price because we are penetrating low customers in terms that they are lower - they are not so big as the ones that we have in our portfolio. Just to prove that that is, the average ticket now is around R\$2,500 per transaction. Until two quarters ago, it was R\$3,000. So what you're saying that these options is very good for the merchants, because we are lending - lending is not the case because we are anticipating. But they are anticipating something that with R\$500, R\$300, without being necessary to go to a bank or even to go to a factoring that's much more expensive. Your question about the funding costs, no, our funding costs didn't increase at all. Just to remember, when we launched the bond, it was the lowest interest rate ever in the history of Brazil, 3.75% (31:12), and if you consider the spread today, it's almost the same thing in terms - related to the bonds. And what we are using is our cash, also to help in the growth of the prepayments. So the funding costs - and by the way, now we have a separate line that indicates how much we are anticipating for the issuers. About...

### Q - Mario Pierry {BIO 1505554 <GO>}

Sorry to interrupt there, so just to clarify this point, I was looking at your press release on page eight where you break down your prepayments of receivables, and you show your funding cost is up 35% year-on-year, sure. And this is my point, here I think also includes some costs that you incur with the banks, not necessarily related to your bond.

### A - Rômulo de Mello Dias

Okay. But sorry, you're right, but the cost of fund here is not cost. Here is what you are - it's the funding that was increased.

### A - Clovis Poggetti {BIO 16529642 <GO>}

The point here, Mario, is that that Rômulo just mentioned, the answer is directly related to the usage of our own cash. Okay. Holding the 30% in terms of dividends, this is one of our main sources in terms of funding. The balance that Rômulo also mentioned in terms of how much we had prepaying our receivables with the issuing banks on September 30, in the total amount of R\$3.4 billion.

Also please don't forget to take into consideration we announced that September 30 is when we pay dividends. So we used it in this quarter with cash to pay dividends and then this last day of the quarter, we prepay our receivables, presenting this balance. Okay? So two different things, one, the usage of our own cash that with the passing of time becomes more and more important as a funding source. And two, despite the fact that the balance in September 30 is R\$3.4 billion, this is more related to the payment of dividends, then let's say company raising money to prepay.

### **A - Rômulo de Mello Dias**

And another point, Mario, I think you are correct, because to say cost of funding is not very well appropriated. Maybe we should clarify here about what happened that SELIC interest rates, it was higher. So when we fund our transactions with the issuers, is a percentage of the SELIC or CDI, exactly the same as you had last year. So here we are talking about the funding, there too it was necessary to increase, because we fund the transactions with the issuers.

### **A - Clovis Poggetti {BIO 16529642 <GO>}**

And one last comment, Mario, LaBarta just called my attention here, that the table on page eight is the managerial analysis. So what we consider as a funding cost here is 104% of CDI, over every Real that we prepay with merchants. Okay? So, in this case, with regard to this table, the answer would be directly 100% related to the usage of our own cash.

### **Q - Mario Pierry {BIO 1505554 <GO>}**

Okay. So then just to be clear, what I was trying to get to is basically you said you've been able to increase the rate you charge your clients, because you are penetrating smaller clients now. And then on your funding side, you're still getting funding from banks at 104% of CDI. The banks have not increased this cost for you? Is that right?

### **A - Clovis Poggetti {BIO 16529642 <GO>}**

Yeah, that's right, and even lower, Okay, 104% is the managerial number as Roberto (35:18) very good point, is just to provide you an idea, because we're calling revenues, gross revenues from clients, and at the end of the day it's not gross revenues, because it's the money that you charge from the merchants, so it's not the spreads.

So, it's the reason why we decide to provide the managerial information, considering that if you have 100% of the transactions funded by third parties, what would be the net revenue? What would be the spread? As a matter of fact, from an accountant perspective, it's even higher, because the cost of capital didn't appear as a cost. So I don't know if with this kind of information it became more clear for you.

### **Q - Mario Pierry {BIO 1505554 <GO>}**

Yeah, no, I'm going to call Roberto (36:05) afterwards as well, just to be clear. And then, if you could discuss how do you think that both businesses are developing over the medium-term?

FINAL

## A - Rômulo de Mello Dias

Yeah. I think you make an interesting point comparing acquiring to prepayments. I would say that when you talk about margins, it's important to understand that we should compare apples-to-apples, so we are right now in a situation near 2014 and as well near 2015 and some things in 2016, that we are investing to have the best platform, the best solution for our customers.

So in this regard, we said and we stressed this point, we let's say said to the market that the cost and expenses should increase because of that. About the growth for sure we expect that the prepayment will grow more than acquiring business per se. Because there is a challenge in terms of how big we are and as well about the other players that are participating.

## Q - Mario Pierry {BIO 1505554 <GO>}

Okay. And Romulo, do you have a target that you think would be appropriate for the prepayments to represent of your bottom line?

## A - Rômulo de Mello Dias

No, no. We don't have a target but the target that you have, that we should continue to increase prepayment and as well the acquiring business. But there is no breakdown Okay. I want to have 40% or 50% or 30% coming from prepayment. The number will come as they are.

And we are, as I said, three years ago that we wouldn't see one reason why we shouldn't reach the same levels penetration after learning how to deal, how to work with the product. And I think now the company is mature, not in terms of the growth of the revenues. We continue to see double digit growth for prepayment. But we are talking about, let's say, the knowledge and how to work well, what's necessary to be done, so on and so forth.

## Q - Mario Pierry {BIO 1505554 <GO>}

Okay. Thank you very much.

## Operator

Our next question comes from Jorge Kuri with Morgan Stanley.

## Q - Jorge Kuri {BIO 3937764 <GO>}

Hi. Good morning, everyone and congrats on the numbers. I have a big picture question on how you think about your business, how should we think about your business in the context of what has been a weak economy? 2013 was weak for the country overall. GDP growth was below expectations, we began the year with you guys thinking your business was going to grow net income, sort of, like I think the guidance was 7% to 12%, you ended up growing 16%, better than you expected, better than even consensus expected. Certainly, you did not have the expectation of growing earnings 25% this year, and that's

Bloomberg Transcript

FINAL

sort of like the nine months level is that, that has also been way above what consensus was expecting, and I guess above what you were expecting and again in the context of a very weak economy. So I just want to understand how you're thinking about next year. I mean, yes, it will be a weak economy. I think consensus is for GDP of less than 1%. You've been able to weather these last two years delivering really good numbers. And so how do you see 2015? Where do you think the levers are for you to continue to deliver good results, better than what the market's anticipating? And just overall, how do you think about the resilience of your business going into next year and potentially also a weak 2016?

## A - Rômulo de Mello Dias

Thank you, Jorge, for your questions. About the weak economy that you mentioned, as I said, we are expecting a challenging year ahead, but not compared to the other sectors that we face a new challenge.

As you know, in our business we don't assume credit risk, and if we don't have a number for the total sales volume next year, and you said for this year would be something between 16% and 18%, and we are probably - we will close for the industry, not for Cielo, we'll close to the bottom of the range.

Having said that, about next year, I would expect with the information that we have in our hands right now, I would expect a lower range, but not that far from the one that we have in year 2014.

About the leverage, what we could do for next year, I would say the prepayment is very important. Also the rental business, and because we expect that GPRS wireless terminal will continue to increase. Nowadays is 61%, and we could reach 70%, 75% next year, okay. So this would help the revenues that would come from rental, POS, when you rent the POS. So I would say these are the two main drivers in terms of products that would help.

In the case of NGR, it's more challenging because of the let's say, new players participating, and then also in case of - there is also other things that you should take into consideration in order to leverage our business, talking about the topline, other sectors such as health, insurance, education, so on and so forth, and also other regions - by other regions, I mean, we are already in the north, northeast, in the middle of the country. And I would say that our penetration in these regions is higher when compared to our main competitors and moreover, the PCE penetration in these regions are too small compared to southeast and the south. So, southeast and the south to some extent is already, let's say, very well attended, if I can say that. But we continue to see growth for the south and southeast, but not with the same speed, not with the same growth that we are expecting for the north and northeast.

## Q - Jorge Kuri {BIO 3937764 <GO>}

Okay. So next year you still have penetration gains, there is some mix benefits from wireless POS', you're still figuring out how to continue to reprice and focus on spread, on the prepayment business, and hopefully you have lower costs relative to what we saw in

Bloomberg Transcript

2014. So, is it fair to say that it's a year in which you should be able to deliver sort of like earnings growth in the teens, maybe high teens? 25% as you've done this year may be too high, but certainly doesn't seem that 16%, 17%, 18% is far-fetched. How do you react to that?

### **A - Rômulo de Mello Dias**

Jorge, I would say that there is also the benefit – just to conclude your last question, the benefit from the shift from cash to cards, so as you mentioned, penetration will continue to increase. In terms of repricing the anticipation of receivables, I would say it's much more a question about mix, because in the case of big accounts, as I said, we fund with our own capital, and as well with the issuers, and that this fund is totally related to the cost of SELIC, to the cost of CDI, okay?

So, and I have, let's say, hedge if you can say, if you will, a hedge because in the case of big accounts, if I take money from the banks from 1.02%, 1.03%, I'm able to charge exact – if the CDI goes up, it goes exactly the same thing when I charge from the big accounts, is the percentage-wise when I charge from the big accounts. But, with the smaller accounts what we do, we charge a fixed amount, okay, a fixed interest rate, and this fixed interest rate of course is something that is a very good option for the, as I said, for the small merchants.

In terms of earnings, I would prefer not to say anything about that, because last time that we did it was not very well. Maybe it was our fault, but it was not very well-understood, because many things happened. We had, just to remember, we had lower incentives that we paid in last year. We had more things -- the prepayment was a very good surprise. We had our targets in terms – not a target in terms of the breakdown, as Mario asked, but targets in terms of how should we increase. The penetration of prepayment was much, much higher than we were expecting by the end of 2013. So, with this kind of information, what we can say is that, yes, we have some leverage. The industry continues to present a good perspective, even on a macroeconomic scenario that is not so easy, but at the end of the day, this industry will continue to present, let's say, double-digit growth and without credit risk, so the pesos (47:02) is something that continues to be very good.

### **Q - Jorge Kuri** {BIO 3937764 <GO>}

Thank you, Romulo, thanks for the information, and congrats again for the great year.

### **A - Clovis Poggetti** {BIO 16529642 <GO>}

Thank you, Jorge.

### **A - Rômulo de Mello Dias**

Thank you, Jorge.

### **Operator**

Our next question comes from Francisco Cobbs with Taft (47:20).

FINAL

Good afternoon, Romulo, Clovis, everyone. Just two quick questions here, one related to the prepayment business. I'm somehow trying to infer the possible impact from the change in the cash cycle in Brazil in cases that happened. I saw that your breakdown of your prepaid volume are coming from credit installments compared with the prepaid volume from regular credit has decreased, okay. Correct me if I'm wrong, but as I calculated, they came from 76% last year to 65%.

What do you guys think is the - this is a trend? I mean, do the prepaid volume come from credit installments to decrease, or is just - was just this quarter a point of fact? I mean, what is the trend in this breakdown? I think this is important.

And my second question is just, I was very impressive of the evolution in points of sales, especially considering the weak economy and the level of maturities the card business already have in Brazil. So, if you guys can talk a little bit about that as well, and what we should expect in the evolution of clients for next year would be good? Thank you.

### **A - Rômulo de Mello Dias**

Thank you, Francisco (48:47), for your question. Regarding prepayment and the change in the cycle, I think if you were - you were since the beginning of the conference call?

### **Q - Operator**

Yes.

### **A - Rômulo de Mello Dias**

Okay. So, I will not repeat myself about the different scenario that you have here, and also when compared to US and other countries.

Having said that, credit in 30 days represents between something 30% to 35%, Okay. And I cannot say - I would say it's really premature to say something that we would expect to decrease or to increase. If I have to say something today, I would keep as it is, with the information that we have now...

### **Q - Operator**

Right, yeah, and I'm just asking this because I think the prepayment volume coming from credit installments are much more defensive in a scenario where you have a changing cycle. That's why my question.

### **A - Rômulo de Mello Dias**

Yeah, you are completely right.

### **Q - Operator**

Okay, So you do not expect this breakdown to change significantly, I mean...

Bloomberg Transcript

## A - Rômulo de Mello Dias

Today, no. Today we don't expect. I would expect to keep as it is today.

## Q - Operator

Okay, thank you. And just regarding the points of sales evolution?

## A - Rômulo de Mello Dias

Francisco (50:17), can you repeat the question, please? Sorry, and I apologize for this.

## Q - Operator

No, no. It was impressive, you guys evolved (50:23) a lot on the number of point of sales, number of clients basically, quarter-over-quarter, and, I mean, considering the weak economy and the level of maturity we already have here in the card business in Brazil, I mean, just would like to know a little bit more about that, and what to expect for 2015 on this regard?

## A - Rômulo de Mello Dias

Thank you for your question Francisco (50:52). Yes, you are right, what we are doing that we are trying to, I'd say, to reduce the lead time between when the merchant asks for a POS, and when they receive. So we are taking, let's say, a lot of actions in order to reduce this, and this is helping the number of - the increase of POS.

I don't know if you also mentioned about mobile, I don't think so, but I think your question is related to POS, that's right?

## Q - Operator

Right.

## A - Rômulo de Mello Dias

Okay. So it was something that you are doing, and you are right, we increased the number of POS. It's very important in this business to continue to grow with new clients, and because as you know, the number of that, if you will, is really high, because you are talking about small merchants. So gross affiliation is increasing, and because there is some merchants that suddenly disappear because they are not able to keep the business, and we need to, let's say, to invest a lot in this in order to have, let's say, a continued growth.

## Q - Operator

Do you guys believe that two-digits growth for next year reasonable?

## A - Rômulo de Mello Dias

I prefer not to say anything (52:25).

FINAL

Bloomberg Transcript



## Q - Operator

Okay. Thanks, guys.

## A - Rômulo de Mello Dias

Thank you.

## Operator

Our next question comes from Alexandre Spada with Itaú BBA.

## Q - Alexandre Spada {BIO 16687974 <GO>}

Hi, gentlemen. Good afternoon. I have a follow-up question on the possible change in the cash cycle of the industry, and its consequences to the prepaid business. If the cash cycle changes, do you believe it would affect only the regular, single installment transactions, or do you think it would also apply to the multiple installment transactions as well?

In other words, does it mean that the first installment would be received by the merchant, let's say in three days, four days, the second in 33 days, 34 days, and so it goes, from the current scenario where the merchant receives in 30 days, 60 days, 90 days, and so on?

## A - Rômulo de Mello Dias

I would not expect. It's difficult to say, if it happen, if it happen, because there are many things that we need to consider. I would expect that the multiple installments would be affected. Because multiple installments, let's remember, is something that the merchants do directly to the customers.

And they have their, for instance, the private labels, the hybrids, it's very common. I think I mentioned in the last conference call, when you open a newspaper here in Brazil in a Sunday, we see many supermarkets, many merchants selling in 18 installments, in 20 installments.

So the competition among the merchants is really high as you know, and they need to sell. So credit installments is something that, just to put things in perspective, and I know that you know this very well, to replace deposit or check (54:05).

And why it would affect, let's say, the first installment of the credit installments, and this would also affect the hybrids, the private labels, the deposit or check (54:33), the other sources of funds that the customers have when they buy their things.

So, my personal opinion, if it happens it would affect the credit installments, but it's just, let's say, our - with the visibility that you have, it would be, let's say, very difficult to apply just for one product and not for the others, because it's something that at the end of the day they compete.

**Q - Alexandre Spada** {BIO 16687974 <GO>}

Okay. But in this case, do you think there would also be no change in the time it takes for you, the acquirer, to receive the money from the banks? If you're still paying the merchant the first installment in 30 days that means the bank could still be paying you the first installment in 28 days or no?

**A - Rômulo de Mello Dias**

First it's necessary to know what are all the things that I said, who would support the negative floating.

**Q - Alexandre Spada** {BIO 16687974 <GO>}

Huh-uh.

**A - Rômulo de Mello Dias**

This is something that - 1% considered the SELIC, just to have a big number, let's say, almost 1% per month is almost the interchange - is almost the same level of interchange. So, you see that what would be the remaining, let's say, portion of profit? Because let's not forget that if it would happen, the credit would be affected, the consumption and the credit installments, as you know, is something that's not very profitable because they have to allocate capital and they don't charge interest rate. I'm talking about the banks, okay.

And if you want to have more competition, if you want to have more players participate in the market, I would say that's necessary and we are completely in favor of that. It's necessary to let's say to have some kind of visibility in terms of earnings for the newcomers to participate. And if you go to another direction, just for the hypothetical situation, just to put things in perspective; if you go to another direction and you remove a certain part of the business in terms of profitability, at the end of the day, the incentives to have new players is not exactly the same.

And the same thing about us. We are in the north, the northeast as I mentioned during the answer to Jorge Kuri's question, and there are some clients, let's say, that are not very profitable, but I take advantage of the scale that I have, and I go to certain regions because I have scales and I can go there to, let's say, hiring suppliers, hiring logistic companies. And this is much more expensive when you go to the north and northeast of course, because Brazil is a continental country, and if you go there, it's much more expensive when I pay to them, even though that I also can have - I can charge a little bit higher.

So, my impression that if you want to have more competition, you need to avoid all the barriers and to allow the competitors to compete, and if they compete, it's the best way to have a better price, a better service, a better proposal for the clients, for the customers.

**Q - Alexandre Spada** {BIO 16687974 <GO>}

Okay. Thank you.

## Operator

This concludes today's question-and-answer session. I'd like to invite Mr. Rômulo de Mello Dias to proceed with his closing statement. Please go ahead, sir.

## A - Rômulo de Mello Dias

Thank you guys for participating in another conference call results. As usual, we are here to answer all the additional questions that you may have. Have a nice day.

## Operator

This concludes Cielo's audio conference for today. Thank you very much for your participation. Have a good day and thank you for using Chorus Call.

*This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.*

FINAL

Bloomberg Transcript