

Q3 2016 Earnings Call

Company Participants

- Lincon Ferraz, Investor Relations Officer

Presentation

Operator

Good afternoon, ladies and gentlemen. At this time, we would like to welcome everyone to Positivo Informatica's 3Q16 Earnings Conference Call. Today we have with us Lincon Ferraz, Investor Relations Officer. We would like to inform you that all participants 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 have been accessed through the company's website www.positivoinformatica.com.br/ir. 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'll 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>}

Thank you. Good afternoon. We are here to present the results for the third quarter of 2016, when we recorded our net revenue from mobile phones of 176 million, it's up 149% year-on-year. The company has presented satisfactory results in yet another quarter, despite the highly unfavorable consumption scenario in Brazil. We gained in market share in the smartphone segment, reaching almost 5% in Brazil in the third quarter.

The revenue diversification because of mobile phone made them to represent 43% of our consolidated net revenue. We had a continued reduction of G&A expenses of 36% in the quarter. We reached 33 million adjusted EBITDA with a margin of 8% and we grew our net income to BRL5 million, four times more year-on-year. Also we have strong evolution

in the cash generation project of inventory management and also in the recoverable taxes. We have some news on Africa. We have a new educational project in Kenya, and our net debt reduced by -- to BRL210 million, which is the lowest level since 2012.

I'm moving to page four to have a big picture of the market. In the PC segment, the demand is still weak, it's falling 33% year-to-date. In the retail, there is a slow lower inventory turnover because of the recession here in Brazil. Unemployment rate is almost 12% is the highest level since 2012. And the Government market also is weak. There is a low flow of bids in the recent months. And also in the third quarter because of the Brazilian electoral regulations we could not deliver some equipments, so we have this one-off effect.

Mobile phones also is reducing but a little bit less. This category has been less affected by the crisis, because people here in Brazil consider mobile phones as a primary necessity. So the company actions to deal with the scenario was to focus on mobile phone. We managed to grow a lot, as I mentioned, 150% year-on-year in terms of net revenue. The market share gains and the launch of Quantum MUV and Positivo Twist smartphones in the retail, the two products represented over 40% of mobile phones revenue and mobile phones offset the drop in the revenues from computers.

Moving to page five, we can see the evolution of our market share in Brazil in the smartphones. We've reached 4.7%, up more than 2 points year-on-year. And as you can see in the chart in the right side, mobile phone market in Brazil is a \$10 billion market, almost three times more than the PC market in the country. So our market share is too small. There is room to grow and it is very important because each percentage point in this segment worth more than each percentage point in the computer segment in Brazil.

Moving to page six, we can see the main launches of the quarter. We have Quantum Fly is our high-end product for the Quantum line. This is the First Deca-Core in Latin America. It's a very competitive price below BRL106,000 [ph]. We have very good specifications. As I mentioned, Deca-Core, 3GBs of RAM, android Marshmallow, we have a very good screen.

And in the right side, we have a very competitive product under Positivo brand. This line has products with more internal storage. There are another line with more front camera for selfie lovers and we have another line with 4G connection. All this products are below BRL700 in Brazil which is very, very competitive.

Moving to the next page, we can see the company actions to reverse results. Beginning with the margins, margins are increasing quarter-over-quarter. This is mainly because of the reduction of inventories. We are not giving discount anymore. So we have a better positioning in terms of price, and also we have some plans to improve variable cost in the company such as after sales and production and so on.

G&A expenses reduced by 36% year-on-year -- I'm sorry 50% year-on-year and we are now running at BRL12 million which is very significant because of the high inflation that we have in Brazil, and we are very happy to keep this number in the coming quarters. The

projects to monetize the recoverable taxes is going fine, we are now at BRL60 million. Our forecast for the year is BRL80 million, so we are on track. And the excess inventory is now at BRL66 million, it's down almost 200 million year-on-year, so it's a fantastic reduction.

Moving to the next page, page eight. I will give some color on the outlook. So for the fourth quarter, we expect revenue increase mainly because of the continuous growth in mobile phones. We expect to keep the triple digit growth base that we have been giving in this year. Government, there is a resumption of deliveries after the election. So we have a good revenue to recognize in the fourth quarter, around BRL100 million. And the retail offices [ph], there is a seasonality at the end of the year, because we have Black Friday and also the Christmas. So we have everything should perform well in terms of revenue in the fourth quarter.

Another thing very important is our expansion in Africa. We have a good news. In Kenya, we closed a new contract to deliver educational tablets and laptops. The volume can reach up to 300,000 device or up to \$100 million. These are the very big contract that we are expecting delivery in November. We expect to close this project in the second quarter of 2017. The profitability in the Brazilian PC market should remain good. We managed very well the inventory. So we don't expect to give much discounts in the next months.

VAIO brand is doing well in Brazil. We launched it in Argentina in September, and we are now preparing to launch in Chile and also in Uruguay. Our new startup company, Hi Technologies is a medical products, is preparing to launch its products in the first quarter 2017. We expect a big launch, very strategic for us, it is a segment with good margin. So we are investing a lot of effort in this launch. And finally, we will migrate the production of batteries and also motherboards that are currently in Curitiba to Manaus. So this will help us to monetize more federal tax.

Moving to the financial results. In the page 10, we can have some color on the sales. Our volumes increased a lot in smartphones over 500,000 units in the quarter, and remain flat in feature phones. For us, it's more important to grow in smartphones because this segment have a big demand in the long-term, and feature phones is a product that in the coming years will be a niche market, so it's not so interesting.

PC segments fell. As I mentioned, we have a recession in Brazil. Market is falling over 30% year-on-year and that's why our volumes dropped by 37% in the retail. Government sales is up a little more because of the elections. We saw a reduction of 75%. But in the fourth quarter, it should be a resumption of deliveries and we will have a rebound on the sales.

Moving to page 11. Net revenue totaled 414 million in the quarter, in nine months it's almost flat at BRL1.3 billion. The main highlight here is the mobile phones, represented 43% of consolidated net revenue. It is very important diversification for us. And opening the net revenue by channel, you can see that we grew revenue in the retail and corporate, both by 20%. And the only segment that we saw a reduction was government as I mentioned because of elections and low flow of bids that we saw in the past months.

FINAL

Average prices in Brazilian currency dropped a little bit in the third quarter because of our currency appreciation against dollars, except mobile phones that increased by 27%. This is due to the increased mix of smartphones in the sales and also the growth of Quantum brands which is our high-end product in the sales mix.

Moving to page 12, we can see COGS and also selling expenses. We can see a big improvement in 2016 when compared to the last year because of the -- we don't need this year to sell off things entirely. So we have a lot of promotions in third and fourth quarters, big discounts to get rid of the excess inventory. This project ended in the first quarter of this year and now in the second and third quarters we don't have any more relevant excess inventory.

There is also an impact in the COGS. Because in the third quarter, we saw the last two retail is very low to government, we see in the selling expense an effect that this sale to retail consumes more marketing expense. So it's important to analyze cost and selling expense together. So that's why we saw 2 percentage point increase in the marketing expenses. G&A expenses, as I mentioned is doing fine. We kept the same value that we saw in the second quarter, we reduced by 36% year-on-year. So the recurring expenses, excluding depreciation, amortization, R&D and also the non-recurring expenses. We are looking forward to keep this number in the next quarters.

Moving to page 13. We can see the operational results. Adjusted EBITDA reached BRL33 million, representing 8% margin, the same margin that we saw in the second quarter and much better than we saw one year ago. This is the result of the improvement in our operation and the growth of mobile phones and the projects to improve efficiencies in the variable costs.

The financial result was negative by 20 million. It was impacted by the exchange rate variation which brought to us expense of BRL5 billion. Excluding this, looking only the financial revenue and expenses, it was 15 million flat year-on-year. We registered a net income of BRL5 million. Most important, we can see in the year-to-date figure that we are now at BRL80 [ph] million reversing the net loss that we saw last year.

In the next page 14, we can see the cash flow. Here it is very interesting because we can see the effect of the cash generation projects such as the recoverable tax bringing to us 60 million in cash. Working capital is a negative of 19 million, but this is mainly because of receivables, we have increased payment term -- receivable term from our clients and that's why we have BRL19 million reduction in the cash flow. We also have some investments to move the production from Curitiba to Manaus, we moved the PCs and tablets. Recently we have moved smartphone production and now we are moving the batteries and motherboards production to Manaus. So all of this changes in the factories are having extra CapEx for this year and these are non-recurring. Putting all together, we decreased in debt by 54 million year-to-date.

And we can see in the next page 15 that net debt reached 210 million, this is the lowest level in four years. We are very happy with that and we expect to keep generating cash.

We know that our value in the stock exchange is very linked to our debt, and we are doing all the effort to reduce more, the net debt.

Moving to 16. Here we have -- the share performance is very interesting this year. The most important thing in my opinion is the increased liquidity in the -- of the stock. We are having right now averaged BRL2 million in daily volume in financial terms, it is three times more than we used to have last year. So we see more interest of people and the share is responding also increasing by 150% year-to-date.

So that's it. I end my presentation here and open to Q&A section. Thank you.

Questions And Answers

Operator

The floor is now open for questions. (Operator Instructions). It appears we have no questions at this time. I'll turn over to Positivo Informatica for final considerations.

A - Lincon Ferraz {BIO 18660463 <GO>}

We are going to have a presentation of results for the fourth quarter next March, so I'm looking forward to see you guys and have great news from the company. Thank you very much, and good afternoon for all.

Operator

Thank you. This concludes today's Positivo Informatica's earnings conference call. You may disconnect your lines at this time.

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.