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Bloomberg Transcript

Q2 2014 Earnings Call

Company Participants

- Carlos Alberto Bolina Lazar, Investor Relations Officer
- Frederico Brito e Abreu, Chief Financial Officer
- Roberto Valerio, Vice President of Undergraduate Distance Learning and Centers
- Rodrigo Calvo Galindo, Chief Executive Officer

Other Participants

- Alexander Vitkalov, Analyst
- Bruno Giardino, Analyst
- Diego Moreno, Analyst
- J.C. Santos, Analyst
- Marcelo Ganem, Analyst
- Marcelo Santos, Analyst
- Patricio Danziger, Analyst

Presentation

Operator

Good morning, ladies and gentlemen, and thank you for waiting. At this time, we would like to welcome everyone to Kroton Educacional's Second Quarter 2014 Earnings Conference Call. Today we have with us Mr. Rodrigo Galindo, Kroton's CEO.

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 company's remarks, they are completed, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions) Also today's live webcast, both audio and sideshow, may be accessed through Kroton Educacional's Investor Relations website at www.kroton.com.br/ir, by clicking on the banner 2Q14 webcast. The following presentation is also available to download on the webcast platform.

The following information is available in Brazilian reais, in accordance with Brazilian's Corporate Law and Generally Accepted Accounting Principles, BR GAAP, which now conforms with the International Financial Reporting Standards, IFRS, except where otherwise indicated.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of Kroton 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 company and could cause results to differ materially from those expressed in such forward-looking statements.

Now I'll turn the conference over to the CEO, Mr. Rodrigo Galindo, who will begin the presentation. Mr. Rodrigo, you may begin your conference.

Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Good morning everyone, and welcome to the quarterly earnings conference call of Kroton Educacional for the second quarter of 2014. With me today is our IRO, Carlos Lazar; our CFO, Frederico Abreu; and Vice Presidents of Kroton's three business units: Rui Fava of Distance Learning and Centers Undergraduate business unit, Americo Matiello of the On-Campus Undergraduate business unit, and Carlos Pegurier of the Primary and Secondary Graduate and Technical Educational business unit.

Let me start on the slide three with the highlight in the quarter. The first thing I'd like to talk about is the merger with Anhanguera. As you know, on July 3rd, our shareholders approved the merger with Anhanguera to create an even better and stronger company. But even before this approval, we were working on planning this integration. The process is going very well and at the end of today's presentation, we'll give more information on the progress we made. But for now, I can say that we are very satisfied with the results so far.

Remember that the merger happened after the end of the second quarter. So the results you see here today reflects the accounting practices of each company and we will begin to report on a consolidated and normalized basis starting at the third quarter.

So let's take a look now at the highlight of Kroton and Anhanguera financial results, starting with Kroton stand-alone. I think the first quarter -- the second quarter brought another round of very strong results for Kroton. For sure, the main reason for this performance was the status [ph] of the enrollment and re-enrollment process for the first semester.

Other factors that made delivery of these results were efficient informing classes, the other roll out of the process to include Distance Learning classes in 20% of the on-campus curriculum and rigid control of costs at both the units and corporate levels. This strong operating performance supported very strong financial results as well reached EBITDA of BRL326 million with EBITDA margin 45%, and adjusted net income of BRL286 million with net margin of 39.5%. In the year-to-date, EBITDA was BRL657 million with EBITDA margin of 47% while net income was BRL576 million with net margins of 41.2%. During the presentation, you'll see just how strong these numbers were (Technical Difficulty) results.

Cash flow was also strong in the quarter with cash flow after CapEx of BRL226.6 million which represent an EBITDA to cash conversion rate of 82%. And in the year-to-date, cash flow after CapEx was BRL443 million and EBITDA to cash conversion rate of 67.4%.

In slide four, you can see the highlight of this quarter at Anhanguera. This is the last time that the Anhanguera results will be reported in separated way and with different accounting criteria. In the third quarter, we'll be reporting in accordance with the criteria and template adopted by Kroton. Anhanguera's EBITDA in the quarter was BRL91.8 million with margin of 18.1%. In the year-to-date, EBITDA was 245 million, growing 15.1% year-on-year with the EBITDA margin of 23.4% in line with the first half of last year.

Adjusted net income in the quarter was BRL49.8 million with net margin of 9.8%. In the year-to-date, net income was 156.1 million, growing 32% on the same period last year. Adjusted net margin was 14.9%, including 1.8 percentage points from the first half of 2013.

In the year-to-date, operating cash flow before CapEx was BRL241 million, growing by 112% on the year ago period. And operating cash flow after CapEx was BRL170 million, growing 183% on the first six months of 2013.

The results of both Kroton and Anhanguera already given a view [ph] of just how solid [ph] the new company is. And this is shown even clear over today's presentation as you will see in more details on our performance.

I now invite our IRO, Carlos Lazar, to present Kroton's financial performance in the second quarter of this year.

Carlos Alberto Bolina Lazar {BIO 17238206 <GO>}

Thank you, Rodrigo. Well, starting from -- talking about the results of Kroton. Let me also refer that the next few slides show the financial performance of the company standing alone. So in other words, with how [ph] the impacts of the Anhanguera merger.

So starting with the slide six, we can look at only the on-campus postsecondary business performance; the net revenue, gross income and operating results. The net income in the quarter grew 52% year-over-year, mainly due to the growth of the paying students in the period, which was increased by the recognition of revenue from prior period for around 20,000 students of enrollment during the quarter.

Revenue in the quarter was also impacted by the higher average tickets and by revenue from Pronatec in the amount of BRL17.6 million, while the income was BRL209 million, which brought margin increasing 13.7 percentage points year-over-year due to the capture of efficiency and quality gains and our careful control of cost. In the same way, operating income grew 133% with operating margin growing 17.2 percentage points to 49.7% also due to the control of operating expenses.

In the slide seven, you can see the performance of the distance learning business in the quarter. Net revenue was BRL209 million, up 43% year-over-year driving -- driven mainly by student based growth. And the gross income grew 55% with gross margin of 79%, 6.3 percentage points higher than the same period last year. This was actually supported by the projects to capture efficient gains and economies of scale. Finally, the operating income in the segment grew by 55% year-over-year with operating margin of 63.1% or 4.8 percentage points higher.

Next slide eight, we show the financial performance of the primary and secondary education business (inaudible) As mentioned in the release, the business was impacted by earlier than unusual sale of collections for the second quarter due to the World Cup. So in other words, part of the (inaudible) for next quarter, the third quarter was already realized and booked in the second quarter. So now we can expect that the third quarter should be negatively impact since the start of the revenue expected for that quarter was already have been recognized as I mentioned.

So the results of that the primary and secondary business posted net revenue growth of 81% compared to the second quarter last year. And the gross income reached BRL23 million and operating income BRL8.5 million, considering that both were also impacted by the revenue growth in the strong evolution revi [ph].

So going to the slide nine, we show the EBITDA net income in the quarter -- actually the EBITDA in the quarter and also in accumulated basis. Adjusted EBITDA in the quarter was BRL326 million with margin of 45%, expanding 14.1 percentage points year-over-year due to the stronger performance of our business, the ex-effect of our student reporting process and the capture of our operating efficiency. The first half results followed the similar path with EBITDA reaching BRL658 million and the margin expanding 9.6 percentage points to 47%. More clear that the EBITDA was adjusted by non-recurring items of BRL12.3 million in the year-to-date, which are basically expenses related to the Anhanguera merger and some integrations that we are conducting.

On the slide 10, we show the net income in the quarter and the year-to-date and here the adjusted net income in the quarter was BRL286 million with margin of 39.5%. Now if you also that -- the net income and adjustments includes not only the non-recurring items that I mentioned, but also the amortization of intangible assets from the acquisitions that we made in the past. Finally, in the year-to-date, net income grew 93% with net margin of 41.2% representing strong improvements from a year ago period.

I'd now let our CFO, Frederico Abreu, to continue the presentation.

Frederico Brito e Abreu {BIO 16674822 <GO>}

Thank you, Carlos. Good afternoon, everyone. So moving to page 12, you can see on the next four slides, the performance of working capital, accounts receivable and PDA, the provision for doubtful accounts.

On the next page, is that exclusively for Kroton, so excluding the effects of (inaudible). Note that like in the first quarter reported these number are pro forma and this means that they include repurchases of FIES credits for the quarter of around 123.2 million. This credit was scheduled for June and due to the delay in that schedule of any [ph] day, they happens in the 3rd of July. So most numbers that we'll look in the next pages they includes this repurchase and causes [ph] the number to pro forma.

So on a pro forma basis, working capital measures in days of net revenue posed to the drop of four days from the first quarter this year or from 28 to 24 days. If you look at real numbers or including the delay in FIES purchase this -- there was an increase of a 11 days.

So moving to page 13, we can see the provision for doubtful accounts as a percentage of net revenue for each of the businesses. It's important to mention that PDA is calculated using exactly the same methodology since 2010, and the methodology is based on statistical analysis of historical building [ph] data. So in short, we can see a stability in our historical receivables curve in on-campus and distance learning segments, which once again we was very comfortable to the level of PDA debt we are adopting this quarter.

So on the left-hand sides, we have the postsecondary business in green. PDA in the second quarter stood at 3% down from 3.4% in the first quarter. And this is mainly due to a higher share of FIES students in our base. FIES students have a very low [ph] PDA, so on the mix, we are seeing a decrease mainly because of larger share of FIES students. If we exclude the FIES students, provisioning was stable at 6.4%.

If we now look at FIES students, we recognize the PDA doing two things. The first, we exclude the commission, FGEDUC guarantee fund commission from net revenues and this 5.6%, so this is excluded from net revenues and this provision, a percentage that is based on the risk of future losses that the company assumes. We have 1.5 risk [ph] for all students that participate on the guarantee fund and 16% risk for all students that contracted FIES contracts before 2014, and which have co-signor. So the PDA is a combination of 1.5 risk or 15% risk multiplied by the probability of loss that we allocate to each of these groups.

We are seeing an increase in the proportion of FIES students under the guarantee fund. It's natural that we'll see a gradual decrease in the PDA for FIES. So we are extremely conservative here on these matter. So looking at distance learning business, as mentioned before, PDA is converging to the levels close to those of ex-FIES on-campus and we have a stable PDA at 6.6%.

And finally, the PDA for Primary and Secondary business increased 3.3 percentage point. And this is important to mention, we had anticipation of sale of collections to our school, because of the World Cup as most of our schools received the materials in June, last year they received in July. So we had an anticipation of the level of collections and therefore, our PDA reflects an anticipation of sales for June in the level of provision that we have here on the second quarter of 2014. It's very close to the level that we had in July last year. So that we can expect for the future is the gradual reduction of this percentage to the levels close to historically levels.

So moving now to slide 14, we have the accounts receivables. You can see a total of BRL519 million in the quarter, BBL351 million in postsecondary and BRL111 million in distance learning and BRL57 million in primary and secondary.

If you look at page 15, we can see the average receivable term. So this is an important metric to see how our accounts receivable are evolving compared to our revenues. For all analysis that we see here we can see a positive evolution for a reduction. Starting on the postcamp on the on-campus postsecondary business units, we showed four measures here. The first shows the consolidated accounts receivable, FIES and non-FIES, and we can see a reduction. If we look at pro forma numbers of 16 days compared to last year and three days compared to the previous quarter, which is a positive evolution.

If we split ex-FIES from FIES on the second criteria, we can see also a reduction of 12 days, if we compare from last year. And in the third analysis, if we compare only ex-FIES students, we have a reduction of three days, so ex-FIES with a reduction of three days. And the last criteria, the number four, we always look at FIES and we have a reduction of 18 days. So ex-FIES with a reduction, FIES with a reduction, if you look at pro forma numbers.

If you look at distance learning, we have an increase of 13 days. This is basically the result of a convergence of provisioning practices between all segments of the company's distance learning and face-to-face. Distance learning is at a lower level of days of receivables compared to on-campus. So we expect it's 54 days to increase to a level that is more close to the on-campus days of receivables.

And finally if you look at the basic education, we see an increase, an important increase and again this is a result of an anticipation of the fall of collections, so this level of 111 days is close to the level we got last year in July and we expect this level of 111 days to be reduced over the next few months.

So now moving to page 17, we present you the CapEx. So the CapEx, the capital expenditures, we have two blocks of capital expenditures, one on the left-hand side, is what we call, recurring an expansion CapEx. And this is the day-to-day CapEx and all CapEx from an investment period of one to three years. It's short-term growth type of CapEx.

And on the right side, we have this CapEx plus the special project's CapEx, which are related with more heavy constructions, acquisition of land, et cetera. So bottom line, we've invest a total in the semester of BRL122 million, which represent 8.7% of net revenues. This is the level slightly below what we consider to be our targets of investment what we had in our budget, which is around 10% of net revenues. So we should expect for the next quarters catch up in terms of investment, so that we finish the year with around 10% of net revenues in total CapEx.

Now moving to slide 18, we have debt and net debt. We ended the quarter with BRL489.9 million in cash and marketable securities, this is 37% higher than last year. If we consider only financial debt, we have a positive net cash, total cash minus the financials debt is positive at 91.9 million. And if we include all the short-term and long-term liabilities we have denominate [ph], and debt -- we have a net debt of 111.9 million or around 0.12 times EBITDA which is a very low and conservative level of debt.

And again this -- this already includes the effects of the repayment of BRL150 we done two months ago. So we have a debenture of 515 million, 150 million of this debenture was prepaid, and we should see the benefits of this prepayment over the next month as we have a lower (inaudible) place in the next months. And the original debt, the 400 that remain, it will start being amortized in December 2013. And this is not impacted yet by the BRL483 million in dividends. We paid already 300 in July, and we remained with 183 to pay in August and September, these numbers are not impacted by these dividend.

Well, on page 20, we have cash generation. So in all analysis that we can see here, we can see a very strong cash flow generation. And if we look at this cash flow generation before CapEx, 312 million, which is 98% EBITDA-to-cash. If we discount recurring CapEx, we have a cash flow of 262 million or 82% EBITDA cash or if we discount also special project, we have a cash generation of 243 million, 76% EBITDA-to-cash. And considering the semester after all these investments in CapEx, we have BRL416 million or 64% EBITDA cash, which is a very strong.

(inaudible) all of the numbers that we presented, they were for Kroton standalone. Starting next quarter on the third quarter, we will presents Anhanguera numbers together with Kroton's numbers divided by segments. And this Anhanguera numbers will be presented already using the accounting principles of Kroton as starting already next quarters.

So I now hand over to Roberto Valerio, who is the Vice President of Distance Learning to continue the presentation.

Roberto Valerio

Thank you, Frederico. Good afternoon, everybody. So before I start commenting on the financial and operational performance of Anhanguera, I just want to reinforce that all these figures, they represent the previous accounting practices for Anhanguera.

So moving onto slide number 22, I want to start commenting on net revenues, which have increased 15.6% in the first half of '14 when compared to the same period of last year. This growth was mainly due to the average -- an increase in the average number of students, but mainly due to an increase in the average ticket, especially on the distance learning -- on the undergraduate distance learning business and also on the on-site business. As you can see the on-site business grew 18% in the half, with the 1.9% growth on the distance learning business, this is mainly due to the very strict process that is going on in our prep programs business unit, the LFG business, as I have mentioned in previous meetings.

Moving on to gross profit, the company was able to post improvements in all line in terms of gross margins. We have improved in the on-site business 2.8 percentage points from

43% to 45.8% in the first half of '14, a growth of 1.8 percentage points in the learning center business from 54% to 55.8% in an average for the overall company of 2.5 percentage points growth in terms of margins. Comparing gross profit, the gross profit increased 22% when compared to the first quarter of '13 and 19.7% when compared to the second quarter of '13.

Now moving on to slide number 23, I want to highlight the adjusted EBITDA figures. The company has posted a 15% growth in terms of adjusted EBITDA, reaching the BRL245 million in the first half of '14. In terms of adjusted EBITDA margin, the figure stayed stable at 23.4%, mainly due to a higher expense on marketing and also higher PDA expenses.

On adjusted net income, the company has received in the first half of '14, BRL156 million, a 32% increase when compared to the first half of '13, and we have reached the adjusted net margin of almost 15% from 13% in the same period of last year.

Now moving on to slide number 24, I want to comment on the PDA and also accounts receivable. My first highlight is on the FIES penetration. We were able to improve 30% in the number of students with FIES, when compared to December '13. Our company has reached 145,000 students, a 45% penetration of its campus student base. And this is the main driver that is helping us to further improve the PDA when we compare to the first half of '14 to the second half of '13, a slight improvement from 7.3% to 7%.

The same -- the higher FIES penetration also improved our accounts receivable in terms of our cash consumption from accounts receivable. In the first half of '13, we have consumed BRL95 million and in the first half of '14, this figure has been reduced 33%, reaching BRL64 million. As you also can see the total number of days in account receivable has been consistently reduced in the second quarter of '14, has reached 91 days.

Moving on to slide number 25, I want to highlight our pro forma cash flow. In terms of cash flow from operations, the company has reached BRL241 million in the first half of '14, an increase of over 110% when compared to the same period of last year. Also we have increased our CapEx, reaching 71 million in this first half. This is in preparation for the growth that we expect -- mainly for the growth that we have expected for the next year.

In terms of our cash after investments, the company has reached 170 million, an increase of 183%. And a free cash flow of BRL57 million compared to 7.4 in the first half of '13. Also I want to highlight our net debt, which has decreased BRL115 million, reaching BRL450 million in the end of the first and the second quarter of '14.

Well with that said, I want to hand the call over to Rodrigo for his closing remarks.

Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Thank you, Roberto. On slide 27, you can see the combined pro forma result of Kroton and Anhanguera in the second quarter and year-to-date, remembering that this result is to consider the different accounting practice of each company. The year-to-date net revenue was BRL2.4 billion and EBITDA was BRL902 million with the EBITDA margin of 36.9%, almost 37% of EBITDA margin.

Net income was BRL732 million with net margin of 29.9% and cash flow after CapEx was BRL613 million. Remember, it gives you an idea of a scale that we have achieved with the merge from a 10 point of financial performance.

(inaudible) results by the company during the first six month of the year, we are revising our guidance for the full year.

Let's move to the next slide for our new guidance. Our new guidance for 2014 considers Anhanguera's numbers for the full 12 months, as well as the standardization of accounting is practices starting in the third quarter. So first and second quarter, the original accounting practices for each company, and from the third quarter, the standardization of the accounting practices (Technical Difficulty) the third quarter.

Considering the excellent performance in the first and the second quarter, we have increased our expectation for the three main lines of our results. The expectations for the combined company net revenue is now BRL4.7 billion and the guidance for EBITDA is now BRL1.5 billion with EBITDA margin of 31.9%.

Expectations for net income is more than BRL1.1 billion with net margin of 24%. Regarding CapEx, we maintained the same production where we have already informed previously, 6% of the net revenue for maintenance and organic growth CapEx and 4% of the net revenues for special projects, that means 10% of net revenues in total CapEx.

Let's move to the last slide of today's presentation for my closing remarks, please. As you can see, we have had another very positive quarter with growth in both absolute and relative terms accompanied by significant margin expansion. We also had strong cash flow in the quarter and in the first six months in Kroton and Anhanguera. But we are asserting that the Group's financial result and strong cash generation as a result of the efforts we've been making since 2010, which have all focus on offering our students of quality education.

Only our high quality education model can build strong brands and only with strong brands, we can grow volume and margins like we've been doing for the past three years. And because of this quality education that we offer and the strength of our brands as we made rough, that we can remain optimistic on the third quarter and the fourth quarter of this year, and going forward for the following year.

Second point I'd like to make now is a status of the integration with Anhanguera. Now we've had over a year to planning the integration with Anhanguera, in Kroton, the last three years, we have more than 20 integration process, and in these processes, this is the one that we are more comfortable, because we have more time to make plans. The plan was concluded in June and during that phase (inaudible) our 24 integration fronts, so each one of these fronts, we can do the several activities that starting on day one of the merge and to the end of the integration process that goes on today is the IT integration.

The task has been massive and taken 37,000 hours of work, involving more than 200 managers.

(inaudible) after shareholders approval in the merge that happens in 3rd July, the second phase began, which is recruiting the integration. On July 4th, after the shareholders meetings, a new organizational structure was implemented that already integrated all management team. And the first technology systems will be integrated in this September and the last one will be integrated in June next year. And now work has been conducting on 196 integration products and they are very comfort in their result. And we are really, really sure that we're creating a company that is even stronger and more solid than both companies along.

The third point that I like to cover in my closing remarks is student enrollment and re-enrollment process for the second semester of 2014. We are in the end of the process. Until now we completed 75% of the process, so we still have 25% in the last enrollment. The end of the process, the process is -- to be concluded in 3rd September. We expect a growth in the total undergraduate student base of 10% to 12% considering Kroton and Anhanguera, distance learning and on-campus business, student enrollment and re-enrollments in relation to second quarter of 2013.

So bottom line we expect for our undergraduate base to grow something about 10% to 12% in the second semester of 2014 comparing with second semester of 2013. We remain confident in the current recruiting process and continue to see excellent growth provision for the future.

And last, in view of the excellent performance achieved over the first half of the year, we are certain that 2014 will be a very positive year and that we are under right track to continue growing consistently over the long term by offering high quality education to our students.

Once again, thank you for participation in today's call and we'll now begin the question-and-answer session. Thank you.

Questions And Answers

Operator

Ladies and gentlemen, we will now initiate the question-and-answer session. (Operator Instructions) And our first question will come from Bruno Giardino of Santander.

Q - Bruno Giardino {BIO 15974970 <GO>}

Good afternoon, everyone. Congratulations for the results. I have two questions. Actually, the first one will be you have an estimate for the non-recurring expenses you are expecting from the merger going forward?

And the second question, we have seen good difference in terms of provisions for accounts between Kroton and Anhanguera. I know that there is a difference in the accounting standards for both, but do you think there is room for enhancing Anhanguera's managerial controls for provision? And do you think this line could go down significantly after you take control of Anhanguera's processes and perhaps change best practices on these matters?

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Hello, Bruno. Thank you for the question. It's Rodrigo speaking. About the non-recurring expenses, what we will see in the next quarters, it'll be a different kind of non-recurring expenses. In the second quarter, the non-recurring expenses is not based of the transaction, so banks fees, things like this. On the third quarter and fourth quarter what we will see, it will be non-recurring expenses related by the integration process. That means consulting firms time for the (inaudible) in the integration process, things like this.

So the characteristic of the non-expenses -- on the non-recurring expenses will change, but we'll see increase of non-recurring expenses, because we are just starting the integration process. And of course, we'll have some non-recurring expenses in the integration process. Okay? Frederico will answer the second question.

A - Frederico Brito e Abreu {BIO 16674822 <GO>}

Hi, Bruno. On the second question, if we -- yes, we want to decrease the PDA. So two things. One, if we align the revenue recognition practices, naturally we will already decrease significantly the difference in terms of PDA. So one of the differences why PDA today is different is because the revenue recognition practices of both companies are different. So the first thing we will do is align these criteria both from Ex-FIES and FIES students.

After doing that, and we already have our estimates on the resulting period, we will have a lot of other structural things to do in terms of collection, and other things that we will work of course, hardly to improve not only in Anhanguera, but also Kroton. We still have room to increase and to improve our collection of Kroton, so we also have room and our expectation is still converge more and more collection practices and they will impact indirectly the PDA of Anhanguera.

Q - Bruno Giardino {BIO 15974970 <GO>}

Okay. Very clear. Thank you, Rodrigo. Thank you, Fred. Bye.

Operator

And our next question comes from Marcelo Santos of J.P. Morgan.

Q - Marcelo Santos {BIO 20444938 <GO>}

Good morning. Thank you for taking my question. Actually wanted to ask about Anhanguera. If the migration of two times a week distance learning course to one time a week, which I think happened in the semester, did it result in any fact on intake or in dropouts? This is the first question.

And the second question is, you have discounts on the -- Kroton has discounts on the revenues and this discounts declined a little bit, which led to -- partially led to a ticket increase. I wanted to understand better how much of these discounts are one-side discounts, which you can manage and how much is something that you agreed with all the companies and you don't have room to change? That are my two questions.

A - Roberto Valerio

Okay. So it's Roberto speaking. I'm going to answer the first question related to the changing the academic model for the distance learning business. So no, the answer is no. The change in the academic model hasn't impacted in terms of enrollments and also re-enrollments. But of course, we have made a lot of changes in this business unit, not only the academic model, but also the IT system, the brands, all the business unit and also in terms of commercial efforts and operational structure, we have also made some changes. So I would say that in terms of enrollments, our rate of enrollments is -- was lower than the on-site business, because of this other changes that not necessarily -- because of the academic model that we have changed.

But we are going to see -- for the future, we are going to see a further improvement in terms of new enrollments. We've already seen this in this second-half of the year due to better processes, internal better process.

A - Frederico Brito e Abreu {BIO 16674822 <GO>}

Okay. So in terms of discounts, yes, we are having a benefit in terms of lower discounts. We think that most of the decrease was already achieved. So we reported on the last quarter about four percentage points of improvements in discount. We do not expect this percentage to increase further. We think most of the adjustments we've made are already concluded. And to be precise we are talking about two things, one is the reduction of what we have got -- what we have here got and call, punctuality discounts. So if the student pays before the due days in the past he was receiving a discount. In the future now, we've adjusted that and few students are receiving that benefit. And the second adjustments we've made is to be more precise and more strict in terms of concession of scholarships. Some students who are benefiting from scholarships, they were not eligible to and we are more restricted in terms of concession. We think most of the work was done, so we do not expect with additional benefits on the benefits we already have this quarter on this specific form.

And one important thing that I'd like also to mention, from all the results that we are seeing on each quarter, the only results in terms of revenue that we may consider, not comparable to last quarter -- that in last quarter last year, is on the basic education. And we expect that the basic education representing in total revenues in terms of anticipation of revenue is about 20 million. And this 20 million are part of the revenue that we were expecting for July was anticipated because of the delivery of the materials was anticipated. Okay. And this is important to mention.

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

And just a compliment Frederico's answer about the level of discount, you can consider that we already captured that most important part of the benefits. The benefits that we captured are sustainable going forward, because we -- with the level of discount and this level is to be remain in the following quarter. Okay?

Q - Marcelo Santos {BIO 20444938 <GO>}

Okay. Perfect. Thank you.

Operator

The next question is from Patricio Danziger of Everest Capital.

Q - Patricio Danziger {BIO 6100532 <GO>}

Hi. Good morning. You've mentioned several times that Anhanguera will be reporting in the new Kroton accounting standards. Can you mention, I mean, which will be changes or what are the changes and if we should expect significant lower revenues or EBITDA or which lines will be affected? Thank you.

A - Frederico Brito e Abreu {BIO 16674822 <GO>}

So Patricio, so the three most important changes and we are working hard to quantify all of them, are related to revenues, so revenue recognition criteria. The most important change is related to FIES students. The two companies have different criterias to revenue recognition for FIES student. Kroton is a bit more conservative, so will adopt that. We do not expect that to be a very large effect, but is one of the effects.

The second is PDA. So we will use exactly the same methodology that the Kroton uses, which is based on statistical analysis of collection in building [ph] data, so we will adopt that as well. And the last one is related to contingencies. So these are the three main changes that we will conduct. The guidance that we're presenting, which is important to mention, already reflects our best assessment in terms of all the adjustments we need to do on this three front. So, the guidance that we're providing is already reflecting these adjustments and we should not ask additional surprises from what we've already provided as a guidance.

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Just to compliment, there are normal adjustments and we see these kind of adjustments in all integration process that we conducted in the past. (inaudible), so it's completely normal these kind of adjustments because we're talking about two different companies with different accounting practices and in the integration of these accounting practices, we need to make this kind of adjustment. And all the adjustments that we're analyzing now we already see this -- saw this in the due diligence process, that we conducted in 2013, so there is no new here.

And one final remark, all adjustments that are related to accounting practices, there are difference. And so that they of the approval of the merger, the 3rd of July, there will be quantified in an opening balance sheet, so we'll produce a new balance sheet starting as of 4th of July, and all the historical adjustments will be deflected, will be reduced from this opening balance sheet. So, the adjustments, that we're building on the guidance that we provided to the market is the adjustments starting as of 4th of July 2014. So the past we showed in this opening balance sheet and the future we already quantifying in this guidance.

Q - Patricio Danziger {BIO 6100532 <GO>}

Thank you very much. And just as a follow-up question, you gave a guidance for synergies between Kroton and Anhanguera. So given that there is no accounting standard, should these guidance or synergies be the same or lower due to the accounting standards or not?

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Now, we're keeping -- we've maintained the guidance, that 300 million we've had on guidance we brought, but that's after the merger. It's a very difficult to separate it what is efficient and what is synergies. So what we'll provide to the market is information, information and result that consider all the fact in the efficient area and in the synergy area. So it's very hard to going forward to follow in detail separate what this synergy now operation and what is synergies. So the synergy that we provide to the market was BRL300 million is above (inaudible) and the opportunity that we have. But we believe we have the space to deliver more than this, but in area that we can quantify the opportunities, for example, restructuring of our brand positioning in some cities that we have. We believe we have this opportunity in some municipalities and some cities, but it is very difficult to analyze how much benefits we can capture with this strategy. So this kind of benefit, I'm not considering the BRL300 million, but the part of the synergies that we can quantify we keep the same level in BRL300 million.

Q - Patricio Danziger {BIO 6100532 <GO>}

Thank you very much.

Operator

The next question is from Diego Moreno of Merrill Lynch.

Q - Diego Moreno {BIO 16605588 <GO>}

Hi. Just a follow-up from the Portuguese earnings call. I have a question more specific about the guidance. I was like to taking -- look into guidance and see that, basically on revenues, your -- what you have achieved in the first semester was basically 50%, and in terms of EBITDA and earnings, you basically already achieved close to two-thirds of what is the guidance for the whole year. So in my view, basically, it's worth saying that you're expecting to do basically the same kind of revenues in the next semester that achieving, roughly speaking, just half of the EBITDA in the earnings that you generate in the first semester.

So this difference into the EBITDA in earnings is just a reflection of the adjustments, accounting adjustments that you're planning in the third quarter, because of their accounting practice or we should be more -- care about another issue?

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Okay. Hello, Diego, it's Rodrigo speaking. So no, the most important part of this difference between the performance of the first semester and second semester and not related by the accounted -- integration of our accounting practices. Actually, there's no part of this. What we believe, it's worth, we don't have a lot of synergies in the short-term, so we announced it before, only 20% of the synergies is captured -- will be capture in this first 12 months. We are talking about the six first month in the integration process. So we cannot expect lot of synergies in this semester.

The second thing is we have a lot of other effects in the first semester that changed performance between first and second semesters, for example, the K-12 business. The K-12 business delivers much more results and much more margin in the first and second quarter then second, then third and fourth quarter. So the combination of this factors normally because of the seasonality, we delivered more results in the first semester than in the second semester. Of course, there are space to deliver a little bit more than BRL1.5 billion in EBITDA. Yes, there are space for that. But the number that we have really comfortable to make a commitment with the market of this R$1.5 billion in EBITDA.

Q - Diego Moreno {BIO 16605588 <GO>}

Okay, pretty clear. Thank you.

Operator

(Operator Instructions) And our next question comes from J.C. Santos of BTG Pactual.

Q - J.C. Santos

Hey, good morning, everyone. Just as a follow-up from the discussions that we were having in the Portuguese conference call. You guys mentioned student base growth expectation for the second half of the year of 10% to 12%. I was just trying to play around with the numbers in here and considering the inherent growth that we were already perceiving in the distance learning business, especially in the Kroton business, you too have embedded growth in your student base coming from second year and third year not only for the second half of this year, but also for 2015.

So would it be reasonable to assume that we could have a significant deceleration in the student intake cycle, especially speaking in the distance learning business for the second half of '14, or is there any other variables in the equation that should also change like, for instance, graduation or maybe dropouts given that the student base in distance learning is getting more mature? Thank you.

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Hi, JC, it's Rodrigo speaking. No, we are not seeing a dramatic deceleration of the intake process of the growth of the -- or potential growth of the company. Actually what we expected before and was announced before for the market is something around 10% of data students growing and this is exactly what we announced and to deliver this semester. There are opportunities to deliver more close to 12%. Yes, with that space we will deliver close to 12%, that means 20% more than our previous expectations. This is huge. So we are completely comfortable with the number we are disclosing now.

And how we told in the Portuguese speech, we will wait for -- to be more close to the end of the process to give more details about the enrollment and re-enrollment information separately. So we can't discuss now because we would prefer to be more close to the end of the process -- before 25% of the process is concluded that means we have 25% of the process that are still ongoing. So we prefer, wait a little bit more, three of four weeks to make more -- to give more color of the enrollment and re-enrollment process for the market. Okay. But as mentioned, we are really comfortable with the growth level that we are delivering.

Q - J.C. Santos

Okay, thank you very much for that. But just a second question on the provisioning for doubtful accounts, in the Anhanguera business, I know that Valerio mentioned in his presentation regarding the literally stable level on a per semester base, but when you look into the numbers in the second quarters specifically, there was a deterioration in provisioning for doubtful accounts as a percentage of revenues, despite of increasing penetration of C.S. Just wondering if you could mention something on that regards or is there any additional opportunities here to improve provisioning for doubtful accounts Ex-FIES in the Anhanguera student base? Thank you.

A - Roberto Valerio

Hi, J.C, this is Roberto speaking. Yes, you're correct. There is room for us to improve the PDA. Basically what happened was that excluding the FIES -- there's a mathematical effect, which is basically, as we are growing the penetration of FIES further this year, there is a higher concentration of distance learning students. So this is one impact and the PDA for distance learning students is higher than our traditional on-site students. And also an impact that we have been mentioning for a couple of quarters is that the remaining students outside of the FIES in the on-site education had a worst performance than the historical average.

Anhanguera, we have to bear in mind that according to our Anhanguera's criterion on provisioning for doubtful accounts, we are looking at six months ago actually, because we provision receivables after 180 days. So a lot of these improvements and the new policies that we've been putting into practice as of in the beginning of 2014 haven't been impacting the results yet. So we do expect improvements on the second half going forward. And as Fred mentioned before, we are working to improve it even further on to our appendix offering of the FIES to those high delinquent students and things like that.

Q - J.C. Santos

No worry then. Thank you very much, Roberto. Thank you.

Operator

The next question comes from Marcelo Ganem of Oceana.

Q - Marcelo Ganem {BIO 18357812 <GO>}

Hi. Good morning, everyone. I have a question regarding the level of discounts and scholarships. If we look at the level of discounts and scholarships as a percentage of sales for both Anhanguera and Kroton, we see a much greater level at Anhanguera and it suggest that they see a huge potential for an increase in the average ticket at Anhanguera. Can you comment on that?

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Hello, Marcelo. It's Rodrigo. You're right, so there's a big difference, yes. Remember that Kroton conduct the pricing study, a very extensive pricing study, one and a half year results. A lot of benefits from that pricing study were already implemented, so part of what you see as a reduction in Kroton is the results of that study.

So, as mentioned before, we've reduced punctuality discounts. We are more strict to give scholarship and we are much more accurate in the increases with city-by-city, course-by-course, so all of this intelligence we will take to Anhanguera. We will start the pricing study also for Anhanguera as part of the integration, together with the branding study. And yes, we can expect, it's worth find convergence, not to the same levels because the cities are different. But we can expect the reduction in the level of discounts of Anhanguera, yes.

A - Frederico Brito e Abreu {BIO 16674822 <GO>}

And if we look at the numbers, I mean this could fill in pretty much, all the synergy level that you have indicated so far. Right. Just on this issue.

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Yes. Again, I want to be reinforce, we cannot expect the conversions to the same level. We are talking about different plans, different positioning which is most structural. So we can expect an improvement, but not the convergence to the same exact level if you compare them to mention.

Q - Marcelo Ganem {BIO 18357812 <GO>}

And if we look at the numbers, I mean, this could fill in pretty much all the synergy level that you have indicated so far, right, just on these issues?

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Yes, definitely. Again, I want to reinforce we cannot expect the convergence to the same level. We are talking about different lands, different cities, different positioning and this is more structural. So we can expect an improvement but the convergence to the same exact level. It is important to mention.

Q - Marcelo Santos {BIO 20444938 <GO>}

Okay. Thank you.

Operator

And our next question is from Alexander Vitkalov of Chamber Street Capital Management.

Q - Alexander Vitkalov {BIO 15221869 <GO>}

Congratulations on the strong quarter. I just have a very brief question for you regarding sort of the upcoming pipeline of expansion in the distant learning centers. I think you have about 450 of centers that were approved between your two core distant learning programs, as well as, new campuses that are going to be essentially Greenfield campuses. I was just wondering how are you going to essentially balance that with the synergies that you were extracting between the merger?

And then the second part of the question is just in terms of the absolute growth of the student base, what's the actual number of students you're targeting in these new distance learning centers and campuses over the next five years?

A - Roberto Valerio

Hi, this is Roberto speaking. So in terms of growth, of course, we expect those Greenfields and also the new 448 distance learning center, which is the total number for both companies, to the operational in the next one year and half or two. We don't disclose specific figures related to the number of students, but of course, there is a growing curve and operational learning curve for all these units as well.

Q - Alexander Vitkalov {BIO 15221869 <GO>}

But I guess in terms of the merger itself, are you going to sort of prioritize your sort of -- prioritize synergies and then focus on the expansion or is this going to be happening simultaneously?

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Alexander, this is Rodrigo speaking. No, we have here the skills to run this two strategies in parallel. So besides the integration process, we are running the 20 Greenfields implementation and besides this, we are running this product to implement at 448 distance learning centers. The fact is for both projects, the distance learning centers and the Greenfields, we need to get the approvement [ph] for the Minister of Education, it takes time. In the distance learning centers, we expected at least one year more to have this approvements.

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And for the Greenfields, the first block of Greenfields we believe we are able to implement in the second semester of 2015. So we are running in parallel, but we need to wait a little bit to have the approvements in the meeting from the Minister of Education. Besides the distance learning project and the 20 Greenfields, we have more than 400 new courses in the actual units that we are running parallel too. So we are not losing any growth opportunity, because of the integration, we are doing this in parallel.

Q - Alexander Vitkalov {BIO 15221869 <GO>}

Right. Thanks so much.

Operator

This concludes the question-and-answer session. At this time, I would like to turn the call back to Mr. Rodrigo Galindo for any closing remarks.

A - Rodrigo Calvo Galindo {BIO 17238232 <GO>}

I just want to reinforce that we are very optimistic with the integration process. And I'd like to thank you everybody for participation on this call today. Thank you very much.

Operator

Thank you. This concludes today's presentation. You may disconnect your line at this time. Have a nice day.

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