

Q3 2021 Earnings Call

Company Participants

- Jorge Fontoura Pinheiro Koren de Lima, Chief Executive Officer
- Mauricio Fernandes Teixeira, Chief Financial and Investors Relations Officer

Other Participants

- Fred Mendes, Analyst
- Leandro Bastos, Analyst
- Mauricio Cepeda, Analyst
- Samuel Alves, Analyst
- Vinicius Ribeiro, Analyst

Presentation

Operator

Good morning everyone and thank you for waiting. Welcome to Hapvida's Third Quarter 2021 Earnings Conference Call. Joining us today are Mr. Jorge Pinheiro, CEO; Mauricio Teixeira, CFO; and Guilherme Nahuz, IR and ESG Director.

I would like to inform you that we have simultaneous translation available on the platform. To access it, click on the interpretation button on the globe item that you can see in the bottom toolbar and choose your preferred language, English or Portuguese. For those of you listening to the English translation, note that you can mute the Portuguese audio by clicking on mute original audio. We would like to inform you that this event is being recorded and will be made available on the company's IR website, ri.hapvida.com.br, where the complete earnings release can also be found. You can also download the slide deck either in English or Portuguese from the link on the chat box.

During the company's presentation, all participants will be in a listen-only mode. After Hapvida's remarks, there will be a Q&A session. (Operator Instructions)

Before proceeding, let me mention that all the information contained in this presentation and any forward-looking statements that may be made during the conference about the company's business prospects, targets and future performance of the company are based on beliefs and assumptions of Hapvida's management and on information currently available to the company. Forward-looking statements are no guarantee of performance. 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 Hapvida and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the floor over to Mr. Jorge Pinheiro, who will begin his presentation.

Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Hello, everyone, thank you for joining us for Hapvida's third quarter 2021 earnings conference call. This quarter's results demonstrate once again the robustness and resilience of our business model, as through it we managed to better navigate the pandemic that hit us in March last year. We are glad to see that the second wave of the pandemic in Brazil is almost behind us and we're very proud of the hard work of our 38,000 employees, 15,000 doctors and 15,000 dentists, a team of giants in yet another quarter in which the company was able to fully show the strength of its purpose.

Once again, we were able to serve all of our customers on time with efficiency and all the care that they deserve. We were able to see a significant drop in the volume of COVID-19 related admissions throughout the third quarter and also the beginning of the fourth quarter. The daily volume of hospital admissions, which reached over 200 at the height of the pandemic, dropped to around 5 to 6 per day. The average number of hospital admissions has remained stable at this level since early October. This consistent movement allowed us to safely demobilize all assets that were exclusively dedicated to COVID patients, which involved around 5,000 medical professionals and more than 1,700 beds which were demobilized in August. We are therefore quite optimistic about the operational normalization in the coming quarters and hopeful when we look at the progress of vaccination in Brazil which continues to advance with great acceptance from the population.

Starting off now with the presentation on Slide 3. Net revenue was BRL2.6 billion, up 20.3% year-over-year, a strong organic growth in our client portfolio and also with consolidation of acquisitions such as Medical, Sao Jose, Promed and Premium. In the last 12 months, in absolute numbers, there was a net addition of 711,000 healthcare members and a 168,000 dental members, increases of 20% and 5.9%, respectively.

We remain consistent in our organic growth trajectory in the client portfolio as well, adding 116,000 clients in health plans and 159,000 in dental plans with commercial performance improving quarter after quarter. This quarter alone, we added 29,000 health lives and 64,000 dental lives organically, impressive numbers considering that the market is still recovering.

The beginning of the fourth quarter already shows an acceleration in the retail channels and especially in corporate accounts. We actually have had several contracts already signed, some of them to be implemented in the fourth quarter itself. Another good news is that we have seen a greater inclusion of new members to existing corporate contracts.

Our cash MCR was 67.9%, 1.3 percentage point higher quarter-on-quarter. Now if we zoom into this figure, we will see that there are some important factors that should be

mentioned.

First, the effect of the tail of COVID-related expenses, we had a high volume of admissions in the second quarter and a strong reduction throughout the third quarter. But there is a natural lag in medical bills. In our own network, we are billed within 30 days. But in our accredited network, usually within 60 days and in some cases within up to 90 days. COVID-19 related costs represented 3.4 percentage points of this quarter's MCR. As we demobilized all COVID dedicated assets, as I mentioned a moment ago, the expectation is that COVID expenses become irrelevant from the fourth quarter onwards. In more mature operations of our company, we're moving strongly towards our historical levels of MCR.

Now the second point is the care costs from newly acquired companies that still operate at higher levels. Notably, Promed and Premium in the city of Belo Horizonte. Both of them had an MCR that was above 100% when they were acquired. These two alone contributed to nearly 2 percentage points in this quarter's MCR. Here we're doing a great job adjusting and enhancing our own network, a process that should last around 24 months since we took over. And we're going to bring the MCR for that region down to the same levels as our more mature operations.

The third point is about the Sao Francisco Group. We made this large and relevant acquisition aiming to reach certain financial and operational targets. In terms of MCR, our target was around 65%. Sao Francisco has half of its operation served in their own units and the other half in accredited network units. Excluding COVID effects, we have achieved this target earlier than expected and we still haven't finished the development of our own network in the region, which has several investments in progress, such as new hospitals and emergency units.

Last but not least, we have the negative readjustment of individual plans, which increased the MCR by 0.5 percentage point this quarter. The impact should be a bit more significant in the fourth quarter of 2021 and the first quarter of 2022, as you all know, but it should be fully recovered with the next year's readjustment. Excluding the Belo Horizonte operations only with ProMed and Premium and the negative readjustment of individual plans which represented 2.4 percentage points, the cash MCR would have been 65.5%.

Now, if we exclude all the effects mentioned above, COVID-related expenses, newly acquired companies that operate with a higher MCR, the negative readjustment of individual plans, then the cash MCR would have been 61.6% in the quarter and 59% year-to-date, a spectacular result in our point of view, which reveals once again our operational discipline. It is important to point out that throughout the three quarters of 2021, even with all the impacts mentioned previously, our cash MCR remained within 60%. This is a unique feat in the country.

Once again, our business model has allowed us to buffer impacts like these, much better than the rest of the market. Note that even including all of the situations I mentioned earlier, our cash MCR in the first nine months of 2021 was 65.3%, much lower than that of

the market in normal periods, which reinforces the strength and sustainability of our business model as well as the execution capacity of our team.

Our SG&A level remained pretty much stable, demonstrating our strong expense control. Our EBITDA reached BRL321.9 million. Hapvida continued operating or generating operating cash throughout all quarters of the year, unlike the other players in the market.

Now moving on to Slide number 4. We remain engaged in reaching the ideal size of our own care network, which allows us to improve the quality of the medical services provided to our members. We closed the quarter with a total of 475 care units, including hospitals emergency units, clinics and diagnostic units; 10 more units than the previous quarter, and we've added 29 units in the last 12 months. As a result, we closed the quarter with 2,988 beds, 852 more beds than in the same period last year, when we only considered ex-COVID beds.

In addition, we now have eight more hospitals that will join the Hapvida's system. Some were acquired and others are in different developmental phases. Some are still in the planning phase and others in an advanced stage of construction. In line with our inorganic expansion strategy, we want the competitive process for the acquisition of Grupo HB Saude in Sao Jose do Rio Preto, State of Sao Paulo, with a portfolio of approximately 128,000 healthcare members. We also announced the acquisition of two hospitals, Madrecor in Uberlandia, Minas Gerais and Hospital Viventi, our first owned asset in Brasilia.

Now moving on to Slide number 5. Here you can see the market share of our health and dental segments at the end of the third quarter of 2021 compared to the same periods in 2020. In the healthcare segment, we had a total increase of 1.2 percentage points with stability in the Northeast region and growth in all other regions. In the dental segment, we successfully continued on our path of sustainable growth. And as a result, we gained 0.2 percentage points of share in the period.

Now Slide number 6. We continue committed to the sustainability agenda. In the environmental sphere we celebrated (Foreign Language) or plastic free July, by starting a project to replace the use of disposable plastic cups and some admin units sparing more than a million plastic cups per year from use and disposal.

In the social sphere, Hapvida has been developing a large work front called the Evolve Project, which encompasses the diverse actions with our employees. We have digitized the entire employee journey and created Affinity and Allied groups to further advance in the topic of diversity. Still in the social sphere, we published Hapvida's harassment and discrimination booklet that reinforces the company's concern about and respect for this topic. Each quarter, we take a new step in this continuous journey, confident that the ESG agenda is crucial for the sustainability of our business.

In October, we announced two capital market operations, an issuance of debentures totaling BRL2.5 billion. Actually the financial settlement is today November the 12th and an issuance of a real estate receivables certificates of up to BRL1.2 billion, an operation

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that is still in progress. The proceeds from these two operations once completed will be used to cover the financial obligations, arising from acquisitions and investments that were already disclosed to the market or that should be disclosed soon in accordance with the company's organic and inorganic expansion strategy.

We have kept a robust balance sheet, which will allow us to continue to participate in the process of consolidating the supplementary healthcare market in Brazil, which is still quite fragmented. The proceeds will also be used to improve our infrastructure and welcome our members with an even higher quality.

Regarding the merger between Hapvida and Grupo NotreDame Intermedica, GNDI, the process is under analysis by CADE, the Brazilian competition regulator and is on its normal and expected course following the initial timeline. The clean teams [ph] with the support of our consultancy have also evolved significantly in their analysis of the synergies in recent months. In M&A, we have a robust pipeline of assets being prospected in different phases different regions of the country and including healthcare operators whether verticalized or not and hospitals.

In integrations, we continue advancing at full steam. America Group was fully integrated and incorporated in 2020. And in 2021, we focused on the San Francisco Group. Now in October, we have successfully completed the largest integration in the healthcare operator segment in the country to date with every single Sao Francisco operation integrated and running on Hapvida's hospital system with the operator now incorporated by Hapvida Assistencia Medica. By the end of 2021 throughout Q4, we plan to integrate medical and Sao Jose Group

And finally, we have also taken advantage of the opportunities created by the market momentum to repurchase shares in order to generate value for our shareholders. We believe that the current share price does not reflect all of Hapvida's values and business opportunities. In October alone, we repurchased 9.5 million shares for total of BRL115 million. In the second half of the year, almost 15 million shares were repurchased totaling around BRL190 million until the end of October.

Now I would like to turn the floor over to our CFO, Mauricio Teixeira who is going to give you further details about the numbers of the quarter and then we'll move on to the question-and-answer session. Thank you very much.

Mauricio Fernandes Teixeira {BIO 19758664 <GO>}

Thank you, Jorge. Good morning, everyone. Jorge has already mentioned the highlights of our results, but I'll give you further details about some of them.

Moving on to Slide number 7, we can see the variation in revenue and its respective growth drivers. Net revenue in the third quarter of 2021 grew by 20.3% when compared to the third quarter of 2020, mainly boosted by the organic increase of 116,000 lives in the health membership and the 159,000 lives in the dental membership, also a 1.3% increase in the consolidated average health ticket. This increase would have been 3.8% if we

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excluded the acquired companies that were not included in the numbers of the comparative period and that have a lower average ticket. We also had a negative readjustment of individual plans reducing the revenue in 20.6% in the quarter and BRL25.8 million year-to-date. If this negative effect were disregarded, the average total health ticket would have increased by 4.7%.

Now, our revenue was benefited from the acquired companies with BRL47.9 million from Medical; BRL42.9 million from Sao Jose Group; BRL125 million from Promed; and BRL46 million from Premium Saude, consolidated only in August and September 2021.

On slide 8, we show the daily volume of COVID admission cases since the beginning of the pandemic, with a strong reduction over the third quarter. Despite this drop, as Jorge mentioned, there was a still high impact of COVID medical expenses due to the lag in the submission of medical bills. Note that in the fourth quarter and up until now, the average daily COVID admission level has remained quite stable at a very low level without any need of dedicated or additional assets to provide service to COVID patients.

On slide 9, we show the breakdown of the MCR in the last quarters and in the first nine months of the year. We can see that the cash MCR was 67.9% in the third quarter of 2021 and 65.3% in the first nine months of the year. Now we can see that COVID-related expenses were BRL87.7 million in the third quarter of 2021 against BRL49.7 million in the third quarter of 2020. This year to face the pandemic, we spent BRL334 million against BRL99 million in the same period in 2020.

We also had an increase in the volume of appointments, tests and elective procedures, not only due to the return to pre-pandemic levels, but also due to the backlog of elective surgeries that's now being addressed. When comparing the third quarter of 2021 to the second quarter of 2021, there was a 20% increase in the volume of appointments, around 9% of increase in tests and around 10,000 additional surgeries. It's important to mention that the surgery backlog was fully addressed throughout the third -- trimester, the third quarter.

Now, another negative impact is the consolidation of higher MCR of acquired companies, Medical, Sao Jose, Promed and Premium that were not present in the comparative period. The MCR of these companies is going down because of the integration initiatives, but they were still higher than our own levels. Just as a reference, these four operators together had a total MCR of 84.2% in the third quarter of 2021. We also had the impact of the collective salary increase in the hiring of new employees, including expenses with personnel at the new units.

The total MCR was 72.3% in the third quarter of 2021 and 69.6% year-to-date, an increase of 11.9 percentage points and 10.8 percentage points year-over-year due to higher IBNR constitution due to the return of elective periods, elective surgeries in the accredited network, an increase in SUS reimbursement that I'll give you further details later, and an increase in depreciation and amortization due to the increase in the number of healthcare units coming both from organic and inorganic growth.

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Now on Slide 10, we have a breakdown of the provision for SUS reimbursement. The net impact of several ReSUS provisions on claim was BRL45 million in the third quarter and BRL162 million in the first nine months of the year. Compared to last year, there was a reduction in the provision levels because of the suspension of regulatory terms. The charges this quarter are more aligned with our recurring SUS reimbursement levels.

On Slide 11, you can see how much the provision for the SUS reimbursement accounts -- accounts for in the company's total claims, which decreased after the first quarter of 2021 considering the denominator of the first quarter of '20 because of the average 12-month lag. For the ABI lot that we received this quarter which refers to procedures performed mostly in the third quarter of 2020, the nominal value is similar to that of the last 15 quarters. But in the last two quarters, the rate was higher due to the claims, which is the denominator, which is below historical figures in the second quarter of 2020 and third quarter of 2020 because of the suspension of elective procedures.

Now on Slide 12, you can see what would have been our cash MCR in the third quarter of 2021. If we disregarded the effects of additional COVID expenses of BRL87.7 million, the highest MCR level of the acquired companies and the negative readjustment of individual plans, the MCR would have been 61.6% in the third quarter of 2021 and 59.0% year-to-date in line with our historical levels, as Jorge mentioned in the beginning of the call.

Slide 13 represent our operating expenses. The selling expenses was 6.6% in the third quarter of 2021 and 7% year-to-date, a reduction of 1.3 percentage points and 1 percentage point respectively compared to the same periods the previous year. These reductions are explained by the reduction of PDD, the reduction in delinquency levels of overdue payments in individual and group plans.

The administrative expenses rate was 10.6% in the third quarter of '21 and 10.2% in the first nine months of the year, an increase of 1.2 percentage points and 0.5 percentage points respectively year-over-year. The main impacts were the collective salary increase, the hiring of new employees, severance pay, legal and consulting fees related to the recent M&A operations including the merger with GNDI.

On Slide 14, you can see our ex-LTIP EBITDA in the third quarter of '21 of BRL321.9 million, a decrease of 37.2% compared to the third quarter of 2020. The EBITDA margin in the third quarter was 12.6%, a reduction of 11.5 percentage points. In the first nine months of the year, the EBITDA was BRL1.1 billion, a decrease of 30.7% compared to 2020 and margins of 15.1%. These comparisons can be explained by the increase in MCR. Excluding COVID care costs, our EBITDA margin ex-LTIP and ex-COVID would have been 16% in the third quarter of 2021 and 17.9% in the first nine months of 2021.

Adjusted net income totaled BRL178.1 million in the third quarter of '21, a reduction of 46.2% compared to the third quarter of 2020 and BRL655 million in the first nine months of the year a reduction of 27.7% year-over-year, mainly impacted by the reduction in EBITDA due to the effects of the pandemic that we already discussed.

On Slide 15, you can see our free cash flow, which was positive by BRL114.1 million in the third quarter, but still negatively impacted by the reduction of EBITDA, which was BRL220.7 million lower. We also had payments that were due in October to the Sao Francisco Group, which had an impact on our numbers.

On the other hand, we had a positive impact of the underpayment of income tax and social contribution. In M&A, BRL114 million in the third quarters were paid for Promed and Premium acquisition. It's important to highlight that while this critical period of the pandemic, the company continued generating operational cash flow throughout the whole time showing the strength of our business model and of our team.

We are now available for the Q&A session.

Questions And Answers

Operator

We will now start the Q&A session for investors and analysts only. (Operator Instructions) Let's now go to our first question from Freddie Mendes. Fred, please unmute your mic and ask your question.

Q - Fred Mendes {BIO 22302086 <GO>}

Thank you. Good morning, everyone. Can you hear me well?

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Yes, we can hear you.

Q - Fred Mendes {BIO 22302086 <GO>}

Okay. I have a couple of questions. The first one, you have already mentioned, but I just want to better understand the numbers for the coming quarters. How confident you are that most of the backlog for elective surgeries caused by the pandemic were already addressed this quarter and that there will be no impact in the coming quarters? That's my first question.

Now, the second question. Gross sales had a slight drop, and when I look at the commission value that was a great increase of 17%. So can you tell me a bit more about that? Was there any the increase in commissions paid by Life to give this boost to grow sales?

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Hi, Fred. Thank you for your question. About the backlog of surgeries, it's quite simple. We look at all the surgery requests by the date of request. And we are very confident that all surgical procedures that were requested and not conducted during the pandemic have now being conducted. There is no backlog left. The good news is that today the

pace of new surgical requests for the mature operations have already gone back to pre-COVID levels. So we have gone back to normal when it comes to elective surgeries.

Now for the acquired companies, especially in Belo Horizonte, which is a new operation, we have a level of request that is higher than our historical levels. But in the next two years, I'm very confident that we can install our own network. And with other actions, we will put this into the same levels of our care indicators, but we're very confident that the backlog has already been addressed and the fourth quarter should not be seen anymore pandemic effects. And if there are any effect whatsoever, they will be irrelevant.

Now I will turn the floor over to Mauricio

A - Mauricio Fernandes Teixeira {BIO 19758664 <GO>}

Hi, Fred. Thank you for your question. About sales commissions, there is a point here that the commissions are deferred based on the average term of the contract. So what we see in the quarter actually refers to sales that were done in the past, it's not directly proportional to the sales of the quarter. So there is no direct relationship here. And in the fourth quarter of last year -- last quarter of last year and the first quarter of this year, we deferred the commissions to the beginning of the year, but this has now gone back to the normal levels. It's in the run rate of what goes in and out in terms of deferrals. And we have a greater mix of individual plan that has a higher commission and the growth in sales there then was impacted by that.

Q - Fred Mendes {BIO 22302086 <GO>}

Okay. Thank you, Jorge and Mauricio. That was very clear.

Operator

Our next question is by Leandro Bastos. Leandro, we will unmute your mic, so that you can ask your question. Go ahead and ask your question, Leandro.

Q - Leandro Bastos {BIO 21416405 <GO>}

Thank you, everyone. I also have a couple of questions. The first one about MCR. I think the message is clear. That's going to be normalized from now on. But can you comment on the evolution of the MCR within the quarter like month-by-month, so that we can have yet another input of the trends from now on?

Now the second question about commercial dynamics. Jorge said that in the fourth quarter, you see a positive trend in retail and corporate contracts. So I just wanted to understand a bit more about what is making you excited here when it comes to sales. You think that the competitive environment is more rational or it is the mix of products or now because the pandemic is a bit more under control? Thank you.

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

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Hi, Leandro, thank you for your questions. About MCR, well, first I would like to say that we're very happy with what happened in the third quarter, because of everything you saw in the market and our company was able to keep it within 60% even with the operations in Belo Horizonte with almost 500,000 lives and the negative readjustment of individual plans and all the COVID expenses in the third quarter -- the second and third quarter were paying for the service provided during the height of the pandemic. And even in spite of all of that, we had a great cash generation and organic and inorganic expansion. This is something that is just unbelievable. The whole team should be praised because we were able to navigate in the best possible way through the pandemic.

Now about the MCR dynamics in the third quarter, it's important to mention two aspects. First, service. In the month of July, we had a high level of admissions. In August, in terms of service, we had demobilization of our assets. We hired over 5,000 professionals, and we had almost 2,000 beds exclusively dedicated to COVID. But in the month of August, we had the demobilization of those assets. And the month of September was the month in which we started to see a low level of COVID-related service stabilized. So, July was strong; in August, we had a reduction in the volume, so we demobilized assets; and in September, we had the stabilization of the COVID-related service at low levels.

Now, when it comes to stabilization. There is a mismatch between service and cash MCR. In the month of July, we paid medical costs of June and May. Now in the month of August, although it was the month in which we demobilized our assets, we were still paying for July, which was strong, and June, which was even stronger. Now, the month of September showed a completely different trend. We paid for the month of August, which was the month of the demobilization of assets. We already entered the month of August with those demobilization, so there was a strong reduction in the cash MCR in the month of this September, which refers to August and July. So within the normal dynamics now, so from now on we expect that the third -- or the fourth quarter be irrelevantly affected by COVID, which is wonderful news.

Now about your second question about growth, we're very optimistic. We are confident that the fourth quarter has everything it takes to be the best sales quarter of the year. We had a first quarter that was almost even, you know then we grew 23,000 lives, in the third quarter almost 30,000 lives, and then the fourth quarter, I believe will be the best quarter of the year. I think we'll go back to historical levels in terms of growth, which is excellent news.

And if we breakdown by channel, Mauricio has just mentioned that retail recovered faster from the pandemic because it's easier for us to sell plans in the retail segment, while the corporate segment was a bit more frozen. It's hard to sell corporate plans during the pandemic, because many patients were hospitalized in ICU and it's really hard to change plans. But the third quarter was marked by many corporate growth opportunities that will come through in the fourth quarter. We have major contracts already signed, one of them with almost 10,000 lives that we had discontinued because it had the wrong price in the beginning of the year. And in the few months they came back to us with a fair price. It was our decision to discontinue this contract, but they're coming back now in the fourth quarter and another two companies as well.

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I remember that in the beginning of the year, we discontinued four different companies for the same reason and three of them have already come back to us. They have already signed contracts, which will start on the fourth quarter. So the corporate channel has great news in terms of growth, with many major contracts already signed.

Now another piece of good news is about the inclusion of new members. Corporate contracts are now at the highest level of inclusion of new members since the beginning of the year, which shows that companies are hiring once again. So they are including new members at record levels now at least compared to the other quarters of the year.

Q - Leandro Bastos {BIO 21416405 <GO>}

Thank you, Jorge.

Operator

Our next question is by Samuel Alves from BTG Pactual. Samuel, we will unmute your mic, so that you can ask your question. Go ahead, Samuel.

Q - Samuel Alves {BIO 18720076 <GO>}

Thank you. Good morning, everyone. Good morning, Jorge and Mauricio. I have two questions here. Both of them about topics that you have already addressed. But I just want a bit more detail. First about organic growth. Maybe talking a bit more about the past than about the future, we noticed an acceleration of organic net additions in the quarter, but this is still a bit timid. So can you tell me a bit more about this? Is this due to higher level of churn in the geographies where you operate? I just want to understand the reason for that number?

Now about MCR, Jorge mentioned in his opening remarks that MCR was naturally impacted by the consolidation of recent M&As and that you expect to take those MCR level to the same level of other more mature operations you have. So you think that when we achieve two years after the consolidation of each one of the assets, you think that the assets consolidated will be running with the same levels of the company, the same MCR levels of the company before these assets were acquired?

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Hi, Samuel. Excellent questions. Thank you. So going back to organic growth, the dynamics that we see, you probably remember that in the first wave of the pandemic, we had a weak sales period. But right afterwards, we saw this heating of the market. And in the second wave of the pandemic, we see a similar behavior.

Now that the second wave is almost behind us, the retail channels have accelerated. But major companies, because we have many contracts with major companies and the corporate channel is very important to us, it takes a bit longer for it to accelerate because the negotiations are harder during the pandemic. And it's also harder to change products during the pandemic. But the negotiations were intense in the second and third quarters. And as I said, we have great news for the fourth quarter and the beginning of 2022 with

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contracts with a large number of lines that have already been signed. But it's important to note that there are regional differences.

The economy is going back to pre-pandemic levels at different paces, like in Sao Paulo and the Northeast, which is a bit faster than other regions. So some regions have heated faster than others after the pandemic. The Northeast has a lot of activity now, the North as well. Some of the contracts I mentioned are actually in regions that are not in the Southeast. So we have now a better balance between retail and corporate channels, which is everything we want. So we're very confident based on what we have had so far and what will still be implemented. And we think that in the fourth quarter, we will go back to historical levels of growth.

Organic growth has always been very strong for us, and that allowed us to gain market share. But we see a great competitiveness of our products in the retail channel, we've always been competitive in the corporate channel, and now we've seen even new opportunities in the corporate channel.

Now about MCR. Thinking about Hapvida's MCR, we should break it down into different clusters. First Hapvida and more mature operations like America, and Goiania, RN and Minas Gerais others that are more mature already. So here we should look ahead with a trend to go back to historical levels of Hapvida's MCR, gravitating around 60%, maybe a little bit more, a little bit less, but going back to the stability.

Now another cluster would be Sao Francisco, due to its size and relevance. And here we have a different dynamics. Our target MCR for Sao Francisco is of around 65%, because half of Sao Francisco uses an accredited network in which the MCR is closer to 70%. And the other half of Sao Francisco has an MCR that is closer to 60%. So our target MCR for Sao Francisco is 65% for those reasons. And we had already been achieving that which is great news.

And as a reminder, we had defined this target for Sao Francisco to be reached in four years time. And we were able to achieve that in two years time, already achieving than our target MCR from Sao Francisco. But there are still opportunities to improve in Sao Paulo. We have three hospitals that are being built, we have an acquisition in Sao Jose do Rio Preto that will increase the verticalization and lives in the region, the implementation of collection points, a lot of imaging tests in Sao Jose dos Campos, Limeira. We still have a long way to go, but we have already achieved our target for Sao Francisco, which is great news. That would be the second cluster.

And the third cluster then would be Belo Horizonte. These are two companies that we acquired in the region had over 100% MCR and they worked mainly with an open network. Our plan for Belo Horizonte has been very well defined already. We are already implementing it, and we've been decreasing the MCR of these two companies strongly. And for these two companies, we will see a plan to correct the asset, which will take two years.

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So when you ask me how long does it take for each asset, well, we have an individualized plan for each asset. There are some assets in which we achieve the results a bit faster, and others not so much, but we are always very transparent with the market. Sao Francisco, we said for years, but we were able to achieve it earlier.

For Americas, we said 30 months, but we have already delivered in Americas, also earlier than expected. And now we want Belo Horizonte's companies to go to these MCR levels in two years time. We have a great operational discipline. Our operations in incorporation areas are acting at full steam, and in every case, in all of our assets, we were able to achieve our integration and results plan earlier than expected.

Q - Samuel Alves {BIO 18720076 <GO>}

That was very clear. Thank you, Jorge.

Operator

Our next question is by Vinicius Ribeiro from UBS. Vinicius, I will open your mic, so that you can ask your question. Vinicius, go ahead.

Q - Vinicius Ribeiro {BIO 19720178 <GO>}

Hello. Good morning, everyone. Thank you for taking my question. I actually have a couple of questions. First, about the fourth quarter. What is the ticket dynamic and price negotiation in light of the last 18 months and everything that happened with frequency, postponement of readjustments and so on and so forth?

Now my second question. Jorge just mentioned the different regions. Can you tell us about the growth expectations by city for 2022, so ticket, competition and maybe the launch of new products as the assets are not that busy with COVID-related cases? Thank you.

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Hi, Vinicius. Thank you for your questions. About ticket, what should we expect? New sales, we have implemented two readjustments this year. One, in the first quarter, around 4%, and another one in the beginning of the second quarter also around 4%. So new sales comparing to the same period last year will lead to ticket increase of around 8%.

Now about the membership and group plans, so small businesses, affinity groups, we've seen something around 8.14, that's the average readjustment that we've had throughout the period. And now finally when it comes to individual plans, this is what you all know, we are giving back to users this negative readjustment that will be offset, But we also have another adjustment next year starting in May 2022. So this is the price dynamics there in terms of average ticket.

About the growth per city or per place, even in cities where we have a high penetration, even in those cities, we believe we'll be able to grow. But the targets are personalized. We

have a target for Goiania, a target for Anapolis, a target for Manaus, Fortaleza, Recife, Ribeirao Preto, Joinville, Belo Horizonte. We have different targets, depending on the penetration we already have in that location, our market share and our own network capacity. We're usually more aggressive when our own network is already ready and running. So it's a very detailed plan, and I wouldn't be able to tell you city by city because within regions we also have different targets depending on all of those variables.

And also as a reminder, these two readjustments that happen every year are coming to our operations. So we always break it down into two annual adjustments. Rather than having an 8% adjustment in January, we'll break it down into two readjustments of 4%, so that users are not that impacted.

Q - Vinicius Ribeiro {BIO 19720178 <GO>}

Perfect. Thank you very much.

Operator

Our next question is by Mauricio Cepeda from Credit Suisse. Mauricio, we will now unmute your mic, so that you can ask your question. Go ahead.

Q - Mauricio Cepeda {BIO 21783651 <GO>}

Thank you. Hello, Dr. George, Mauricio, thank you for your time. This is Mauricio Cepeda from Credit Suisse. I'm not going to be very creative. I want to go back to topics that were already mentioned, but from a different perspective. When it comes to organic growth, can you give us a bit more idea about what is going on in the field? Who are you competing with for these organic lives, not in the corporate or in affinity because individually you have a certain advantage, but who is competing with you? When we see these cancellations, are you been beaten by someone else?

And my second question. I have another two question. So the second is about verticalization. What are your plans from now on to create your own network, where do you have new plans for a more comprehensive verticalization?

And my third question about the backlog itself. You have been monitoring by the date of request, I know. You mentioned this. And now that people are doing their screening tests, do you think that they can lead to another backlog of procedures for the future?

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Hi, Mauricio. Thank you so much for your question. I'll try to answer all of them. But if I don't, please remind me. So, first, about the competition in organic growth. So what we notice was the following. Among the large players, we saw no different behavior than compared to what we are used to. The last year, we saw the postponement of elective procedures, especially in small and medium businesses. But locally and with a higher level of aggressiveness like in city A, B and C, we saw someone being more aggressive and small and medium companies or individual plans, but it was an atypical behavior. So

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right after the second wave of the pandemic and especially now that these companies have to give back part of the readjustment for the individual plans.

We noticed that these companies are with a short of breath. So, I see that these small and medium businesses that were a bit more bode [ph] so to speak are suffering now. And this has been bringing us great opportunities from the organic perspective because these players are now having to offset readjustments in other channels, since the individual channel, they have to give back money to users and they have the COVID expenses to pay for. So they're losing competitiveness and trying to offset those in other channels. And that also applies to the inorganic channel.

We have several M&A projects in course [ph], many of the companies that had their negotiations closed, came back to negotiate with us. We have many MoUs already signed, many processes and due diligence. So I think that we're going to go through a period of normalization with the small and medium businesses going back to reality, and being a bit more responsible now. And that will give us great opportunities for organic and inorganic growth.

I do not see any competitor with the capacity to have like a cost structure that can face us in most of the regions where we operate. We've been very disciplined, continued -- and we continued to invest in our model, in our own network, in technology, so that our product is always the most competitive one. I don't see any player with cost structure and balance in between cost and quality that could face us in a holistic manner.

Now about verticalization, we have many, many acquisitions [ph]. Let me give you give some examples. In the Midwest, we are building a hospital in Campina Grande. So, in Brasilia, we just made the acquisition of a hospital and we're going to verticalize in the region there. And we have a hospital in Anapolis and other opportunities. And in the Northeast, for example, we are just delivering a new pediatric hospital in Manaus. We are working on two new hospitals in Recife, also pediatric hospitals and other opportunities. In the Southeast, we have Belo Horizonte, in which we have a plan to implement many of our own units, labs, diagnostic units, imaging, clinics, and we plan to expand our hospital network and the Minas Triangle. We just announced a hospital in Uberlandia, that's how we needed to verticalize our operations there.

And in the country side of the State of Sao Paulo, also many different initiatives, three hospitals under construction, we are also working in the outpatient and lab areas, we are moving firmly towards our purpose. And during the pandemic, this year from January to September, we did 65% in terms of cash MCR even with those many acquisitions and absorbing all of the impact of the pandemic. And that shows the resilience of our model and gives us great competitiveness. There are many projects ongoing and we continue implementing them firmly.

Now about the backlog, we have not seen that happening. We monitor the number of new requests every day, and it's been in normal pre-pandemic levels in recent days. So nothing new there.

Q - Mauricio Cepeda {BIO 21783651 <GO>}

Okay. Thank you, Jorge. Just going back to my first question, in cases in which you have lost lives, are you losing this lives to someone else? Or these employees are not there?

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Well, Cepeda, as I said, we discontinued four companies this year, in the beginning of the year. All of the companies had low price for us and we did not reach an agreement with them. But of those four companies, three of them have already come back to us and signed new contracts. And they had gone to small and medium operators and their cities of origin. So three have come back to us already, and the fourth will come back as well. So we're not losing lives to competitors in the corporate channel. On the contrary, it's now the season to gain market share and beat our competitors.

Q - Mauricio Cepeda {BIO 21783651 <GO>}

Okay, thank you so much. You were very clear.

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

Thank you, Cepeda

Operator

Well, if there are no further questions, we are now closing the Q&A session. Now I would like to turn the floor over to the company for the final remarks.

A - Jorge Fontoura Pinheiro Koren de Lima {BIO 22175271 <GO>}

So we just want to thank all of our employees for the huge effort in facing the second wave of the pandemic. I want to thank our partners and our investors for believing in our dream, which is to offer very high quality care in an affordable manner to all of our customers, in our greatest commitment to our users for whom we struggle on a daily basis. We're very hopeful that the fourth quarter will be wonderful with great growth, acquisition, integrations and going back to normal levels of operations after having gone through this challenging period. So thank you very much and have a great day.

Operator

This concludes Hapvida's third quarter 2021 results conference call. The IR department is available to answer any other questions that you might have. Thank you so much and have a great day.

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