Q4 2015 Earnings Call

Company Participants

- Carlos Alberto Bolina Lazar, Investor Relations Officer
- Frederico do Casal Ribeiro Brito e Abreu, Chief Financial Officer
- Rodrigo Calvo Galindo, Chief Executive Officer

Other Participants

- Rodrigo Gastim, Analyst
- Ruben Couto, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen, and thank you for waiting. At this time, we would like to welcome everyone to Kroton Educacional's Fourth Quarter 2015 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 a listen-only mode during the company's presentation. After the company's remarks are completed, there will be a question-and-answer session. At that time, further instructions will be given.

Also, today's live webcast, both audio and slideshow may be accessed through Kroton Educacional's Investor Relations website at www.kroton.com.br/ir by clicking on the banner 4Q15 Webcast. The following presentation is also available to download on the webcast platform. The following information is available in Brazilian reals in accordance with Brazilian Corporate Law and Generally Accepted Accounting Principles, BRGAAP, which now conforms with 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 earnings conference call of Kroton Educacional for the fourth quarter of 2015. With me today is our IRO, Carlos Lazar; and our CFO, Frederico Abreu.

The year 2015 was a challenging one, with regulatory changes in the FIES student loan program and sharp deterioration in the macroeconomic scenario. Despite this adverse environment, we were able to enhance the company's efficiency and deliver very robust results with the numbers for the fourth quarter, demonstrating the company's solidity and resilience.

I want to start today's presentation with Slide 4, which shows the improvement in the company's results on a pro-forma basis, based on the combined figures for Kroton and Anhanguera for 2014, in other word words, considering 12-month of Anhanguera results in 2014. The main lines of our results also showed progress with net revenue growing 9%. But the strongest growth was in EBITDA and net income. We've adjusted EBITDA growing 28% and adjusted net income growing 30%. The numbers are really very strong with EBITDA margin expanding 610 basis point points from 35.3% in 2014 to 41.4% in 2015 and net margin expanding 540 basis points from 28.5% in 2014 to 33.9% in 2015.

Considering the turbulent scenario we faced in 2015 with the regulatory changes in FIES at the start of the year and an unfavorable macroeconomic environment, Kroton's response was to continue to capture our efficiency gains. Many actions were implemented during the year and I will highlight the most important ones.

We implemented a new academic model KLS 2.0, which allows us to optimize the allocation of students across courses by improving the efficiency of our transformation process and, in parallel, we developed and implemented an unprecedent new tool that uses operational research to carry out this class (4:06) information process with a maximum level of efficiency. In other words, we innovated to become more efficient. We also continue to capture synergies from the Anhanguera merger such as replacing Anhanguera's distance learning model with the Unopar model.

Another important driver of our results was a strategic sourcing project implemented in the 30 procurement (4:30) categories with the most significant impact. All these efforts combined with our rigorous budget control supported improvement in our 2015 results despite adverse macroeconomic scenario and we will take a more in-depth look at all these factors on the coming slides.

Let's go to Slide 5, which shows the performance of the company's margins in the last five years which, once again, reinforce the company's capacity to reinvent itself and capture efficient gains on a daily basis. On the chart on the left, you can see our EBITDA margins, which has grown from 9.80% in 2010 when we began restructuring Kroton to

41.4% in 2015. On the chart on the right, you can see the same evolution in net income with net margin growing from 1.8% in 2010 to 33.9% in 2015.

One important point I should highlight here is that the many efficient levers that supported margin expansion in 2015 continue to create opportunities in 2016, which gives us on a comfortable - which gives us comfortable in saying that we do not see room for margin compression in 2016. This is very important. The opportunity that we still have in 2015 gives us comfortable that we do not see room for margin compression in 2016.

Another highlight is Kroton's strong cash generation in the year of BRL 677 million, which confirms our adequate and conservative revenue recognition policy and supported the company's low leverage. I want to emphasize, once again, (6:20) the challenges posed by Brazilian economic scenario, but our numbers shows that our operation is very strong, is stable and resilient.

But it's not enough to deliver good financial results if we don't deliver good academic results. In the official results published by the Ministry of Education in 2015, 98% of Kroton's institutions obtained satisfactory scores in the General Program Index, IGC. At the start of this year, we've published our latest employee ability survey, which shows that our student's average income after graduation grew by 181% compared to before they started our program, already adjusted for inflation. These regulatory indicators and the employee ability survey gives us confidence that this value creation is sustainable.

Turning now to Slide 6. I'd like to comment on the results delivered in 2015 compared to the guidance given by the company during the disclosure of the first quarter results. (7:25) we ended 2015 beating our guidance in the main (7:28) account lines. Kroton posted net revenues of BRL 5.3 billion with this performance is likely beating by 1% of our guidance of BRL 5.2 billion. Adjusted EBITDA was BRL 2.2 billion, 12.9% above the guidance with EBITDA margin of 41.4%. And adjusted net income in the year was BRL 1.8 billion, beating our guidance by BRL 345 million. And net margin was 33.9% or 630 basis points above our guidance. And the total investment including special products corresponded to 8.3% of net revenue, which is marginally above our guidance of 7.5%, due to acceleration of our greenfield project.

In other words, the 2015 results were truly very positive and we demonstrate that all the efforts we made were essential, while also confirming the effectiveness of our strategy. Let's turn now to the analysis of three very important indicators in our operation, which are dropouts, delinquency and (8:42) and to comment this numbers, I invite our IRO, Carlos Lazar, to continue the presentation.

Carlos Alberto Bolina Lazar {BIO 17238206 <GO>}

Well, thank you Rodrigo. Hi, everyone. I invite you all to turn to slide number 7 to continue to talk about the highlights of the quarter. And as Rodrigo said before, the main factors potentially affecting the education industry during the adverse macro economic scenarios are dropouts and delinquency. And to start with that, in terms of our dropout rate, the message are very good, in both On-Campus and Distance Learning, very, very positive.

In the On-Campus business, we reported a slight improvement in our dropout ratio in comparison of the closing quarters of 2015, 2014. While in Distance Learning business, the rates remain stable. Considering the adverse macro environment that we're facing, I think that the Retention Program which consists of set of projects to reduce dropouts is playing a fundamental role in supporting our good results in this area.

Delinquency, another important indicator, has remained and also stable in both On-Campus and Distance Learning businesses. In the On-Campus business, the (10:04) stabilized at 6.5%, while Distance Learning business has stabilized at 7.4%. These indicators give us even more confidence that even in these scenarios, with more stability, we are taking advantage of opportunities to capture efficiency gains, which are neutralizing the effects of the crisis.

Turning to Slide number 8, I will comment in our average ticket evolution. In the previous quarter, we commented that the average ticket had been impacted by the one-off commercial actions implemented in the new enrollment process for the second semester. And that in the fourth quarter, the average ticket should present the amount of monthly tuitions excluding this impact. While this is what exactly what happened and was verified in the fourth quarter because the average ticket in the On-Campus business grew by 9% compared to the third quarter and too, we believe that to neutralize all these seasonal effects, the best thing to do is to analyze the tickets in the half year basis because this offsets all these changes in the seasonal impact between the quarters.

In this analysis, the average ticket in the On-Campus segment increased from BRL 643 in the second half of 2014 to BRL 705 in the second half of 2015, an increase of 10%. In the Distance Learning segment, the average ticket increased from approximately BRL 236 in the third quarter to BRL 246 in fourth quarter, an increase of 4%, also supported here by the various one-off campaigns (11:54) offered in the third quarter. In comparison to the half-year periods, the average tickets fell by 5% compared to the second half of 2004, basically explained by three factors, the repositioning of prices in certain markets, as we already commented in other quarters. The higher number also of ProUni students and the higher number of 100% web-based Distance Learning students for which the average ticket is lower.

The outlook for the average ticket remains positive for 2016 and I want to emphasize here also that – we are – that the same quarterly seasonality continues to be observed. So, we believe that the first quarter we have a lower ticket compared to the second half quarter as we similar saw in the second half of last year.

And we made also very important – so just to summarize, we made very important solid progress in these three indicators – dropouts, delinquents and prices, which are important to confirm that we have adopted effective strategies and tools for continuing to minimize any impact that we may suffer from the growth (13:11).

So, I'll now begin the comments about all the business that we hold in terms of financial performance. Starting on Slide 10, you can see the financial performance of our On-Campus post-secondary business. Here, net revenue grew by 11% year-over-year, driven mainly by the student base growth, generated by our new enrolment and re-enrolment process, compared to the third quarter of this year, net revenue grew 10%, mainly to the recognition of revenue from around 20,000 students mostly from FIES, who concluded the re-enrollment process after the end of the third quarter, accounting for an additional BRL 60 million in the fourth quarter, but related to the third quarter.

Gross income was BRL 653 million, growing 14% year-over-year with the gross margin expanding 1.3 percentage points driven by the revenue growth in the ongoing capital efficiency gains (14:21), which includes the initial impact from the operation – operational research software implemented by mid last year.

Operating income before marketing expenses increased by 16% year-over-year, with operating margin of 48%. In 2015, operating income was BRL 1.9 billion with operating margin of 49.2%, expanding also here more than 1 percentage point in 2014.

Turning to the Slide 11, you can see the performance of the Distance Learning segment where our net revenue was BRL 283 million, so it was 2% lower than the year before. And in the third quarter, we emphasized that although the performance of the new enrollments in re-enrolment process in Distance Learning business during the second half of last year were positive, revenue was affected by the lower average ticket of the programs as I've mentioned before. And also, at the lower revenue from the graduates and also prep courses that we offer.

Gross income grew 4% in the period with gross margin of 80.1% or 5.2 percentage points higher than year-over-year, which is explained by the efforts to reduce our payroll costs with the convergence of content delivery models at Anhanguera and also by the restructuring of our prep course structure.

The operating income in the Distance Learning before market expenses grew 15% year-over-year with a margin of 64.7% or 9.5 percentage points higher than in 2015. The operating result was almost BRL 790 million (sic) [BRL 190 million] (16:15) with a margin of more than 65% expanding 3.5 percentage points from 2014.

In the last segment, on Slide 12, we talk about the Primary & Secondary education, the K-12 season (16:31) where net revenues grew 16% year-over-year to BRL 42.6 million, mainly due to the good performance of management contracts and own operations as well as very good performance of the learning systems network.

Gross income in the quarter was BRL 23.5 million with gross margin of 55% expanding a very good number of almost 10 percentage points year-over-year, reflecting here the lower costs that we recorded in the quarter. In the same way, the operating result was about BRL 18 million, with operating margin of 42%, also expanding largely from the year before. In the year, the operating result of this segment was BRL 18 million, not as good as in 2014, but with a very good margin, however.

On the Slide 13, you can see the corporate and selling expenses. Here, the corporate expenses were about BRL 90 million or 6.7% of net revenues. So, little reduction compared to a year before, about 1.1 percentage points, basically due to the three factors that I mentioned before but I would like to reinforce. The changes made in the administrative structures after the Anhanguera merger, the corporate restructuring carried out during the last year, especially during the first half of last year, that we're impacted partially in 2015, and also the important reduction in expenses achieved by the strategic sourcing process and also the greater budget austerity.

Meanwhile, selling and marketing expenses as a ratio of net revenues fell about 1.6 percentage points year-over-year, demonstrating the rigorous control of our costs.

And moving on to Slide 14 shows the EBITDA in the quarter and the year. Adjusted EBITDA in the quarter was BRL 518 million, increasing 29% year-over-year, with a margin of 38.9% for expansion of 6.4 percentage points. In the year, adjusted EBITDA was BRL 2.2 billion, growing to 50% comparative 2014, which is the margin expanded about 2.8 percentage points to 41.4%. This performance in the year really confirms the success of the initiatives that is being implemented by the management to capture operating efficient gains and also, the continuously rigorous in the control of costs and expenses in all operations.

It's good to note here that the EBITDA is adjusted by nonrecurring items, which came to BRL 57.6 million and it is mainly involved with expenses with payroll and severance related to the operational research software that we implemented last year, as I mentioned, in the On-Campus business. The impact of this – it was partial last year and will be much more this year in our results. We also expect very good, we mentioned that we expect the total amount of non-recurring items in 2016 should be reasonably lower compared to 2015.

Turning to Slide 15, you can see the performance of net income in the quarter and the year. Net income adjustments include not only the non-recurring costs and expenses considering the EBITDA adjustment, but also the amortization of intangible assets related to acquisitions.

In the quarter, adjusted net income was BRL 409 million with a net margin of almost 31%. And in the year, the net income, which is about BRL 1.8 billion with net margins achieving 33.9% or 1.7 percentage points above 2014. So, I'll now invite our CFO, Frederico Abreu to continue the presentation.

Frederico do Casal Ribeiro Brito e Abreu {BIO 16674822 <GO>}

Thank you, Carlos. Good afternoon, everyone. So, on the next three slides, tracking on page 17, we will analyze our provision for doubtful accounts, the accounts receivable and our average receivable term.

On Slide 17, we can see PDA as a ratio of net revenue for each business, it's exactly the same formats we've been presenting over the last quarter. And before starting, I would like to emphasize that PDA is calculated using the same methodologies since 2010 and is based on a statistical analysis of historical given data and the same methodology was applied also to Anhanguera starting in the first quarter of last year.

And before getting into the numbers, I would like to impart two important messages. The first, you can see stable and relatively conservative PDA levels in our businesses. Second, we can see a high coverage ratio for our accounts receivable. And three, you're going to see later on the presentation the stability in the average receivable term except for the FIES effect that I will mention in a while.

We've maintained also our conservative provision policy in our products and I would like to emphasize our conservative policy also on PEP. PEP is our special installment product that we've implemented in 2015. We are provisioning 50% of all the balance that the student finance is 50% and we are continue to provisioning the same 50% also on this quarter.

And we are also, I would like to also emphasize that we are following our performance indicators on which we got PDA daily. We are also observing the trends in other sectors. And what I would like to emphasize is that our PDA levels are sufficient enough and are already calibrated for a potential deterioration that we may see in 2016 delinquency. Okay. So, our levels are already prepared for a potential deterioration in delinquency.

In any case, we've been working very tirelessly over the last 24 months on many different fronts to continue capture operating efficiency in our collections operation, both in prevention and also on collections. And we believe that these efficiency gains should mitigate a potential deterioration of our delinquency because of the macro scenarios. So, we are doing what we can in terms of efficiency and we believe that we'll mitigate part or total of what we are seeing in our macro scenario.

So, starting on the On-Campus and looking at the numbers now, if we look at the face-to-face (23:51) PDA, we can see on the fourth quarter 4.5% PDA, which is an increase of 0.1% over last quarter. And this increase is mainly due to PEP, which I've mentioned has a very conservative policy of PDA. If you exclude these effects on the right hand side of the face-to-face (24:14), you can see a stability of 6.5% PDA for paying students, so all students except for the PEP and FIES students, stability on 6.5%.

If you look at the Distance Learning on the red bars, you can see that also on this segment, the PDA is stable and this already includes LFG operations, both regulation (24:38) and LFG, so stable as well.

And last on Primary & Secondary education, we have an increase of 0.2 percentage points compared to fourth quarter last year. But this stability, if we compare over the previous quarters, so again stability, both in face-to-face (24:58) on Distance Learning and on Primary & Secondary education. And here, I would like to emphasize that even on a more challenging macroeconomic scenario, we are maintaining and keeping our position and levels stable. We are continuing to be conservative on our provisioning practices. Our accounts receivables coverage ratio is robust. And we are continuing to capture efficiency and synergies with Anhanguera and improving our collection operations.

So moving to page 18, we can see here the accounts receivables already net of PDA in the three businesses. The most important event that impacted our accounts receivable in 2015 were related to FIES. As you remember, we had a strong impact due to the

Normative Rule number 23, a part of our accounts receivable related to FIES were not paid. We already have an agreement with the government so that their accounts receivables will be paid 25% in 2016, 25% in 2017 and 50% in 2018. And this balance of FIES that was not paid in 2015 represents about BRL 725 million and that was the major reason for the increase in the overall accounts receivable.

We already have, for 2016, beyond the agreement for the payment of the balance that was not paid in 2015. We already have the 12 repurchases on the calendar and so, we will, in 2016, get back to normality again in terms of FIES receivables.

So, if we – and I would like to also to emphasize one thing about FIES, we are already accounting for an adjustment to present value because this balance will be paid over two years. We are adjusting our net revenues by BRL 24.6 million in adjusted present value. This is impacting negatively our EBITDA and we are correcting the balance of FIES on a positive side by BRL 12.9 million, which is a financial revenue. So, the net effect between our APV, the adjusted present value and the correction of the balance of FIES is BRL 11.7 million, negative in our recurring EBITDA.

So, moving to the numbers, the accounts receivables totaled BRL 1.6 billion, out of which BRL 1.3 billion is related to On-Campus, BRL 223 million related to Distance Learning and BRL 45 million related to Primary & Secondary business. Out of the BRL 1.6 billion, BRL 1.075 billion or 67% is related to FIES and out of which BRL 725 million is related to the balance that was not paid in 2015.

Now on the next slide on page 19, you can see the average receivable term for each of our businesses. We present here in the same say as we've presented in our other quarters, the analysis for On-Campus, Distance Learning and Primary & Secondary education. So starting with the face-to-face, you can see an increase of 69 days year-on-year. This is mainly due to FIES, the effect as mentioned related to Normative Rule 23 and related also to PEP. So, this 69 days are related exclusively to FIES impact.

If we exclude FIES out of the analysis, which is the second analysis we have here on On-Campus, you can see an increase of 14 days. Why we have this increase of 14 days? If we exclude not only FIES but also PEP from these average receivable term, the paying students, if we look at the average receivable term, only for paying students, we have a stability of 62 days. So, last year, we had 62 days; this year, we have 62 days. So, this 14 days increase is exclusively related to PEP students. This is very good news because we are being able to keep PDA levels stable but also the average receivable term stable for paying students.

And finally if we look at the balance and the average receivable term for FIES student, you can see the significant increase from 51 days to 147 days, 90 days increase. As I mentioned, this year in 2016, we will start getting and receiving 25% of the balance that was due in 2015, plus we're going to have 12 repurchases to lower expectation, is that this average receivable term of 147 days, we'll start decreasing over the next three years converging to what we consider recurring levels of FIES average receivable term in 2018.

On Distance Learning, you can see an increase of 14 days. As in other quarters, we are seeing an increase in the average receivable term of Distance Learning to the levels of On-Campus students. We are seeing this movement over the last 1.5 years. This is not necessarily bad. Why? Because we're being able to keep PDA stable and this very important. We are having an increase in the average receivable term but PDA is stable. So, we are not increasing our delinquency because of this. What we are doing is having the set of campaigns in renegotiation terms with our Distance Learning student, similar to the ones we have with On-Campus student, and this is generating to Distance Learning segments, specifically, financial revenue related to interest and fines, that is very positive. And in 2015, we generated about BRL 39 million in interests, which is 90% higher than last year.

So, the important thing here is the convergence of average receivable term of Distance Learning to On-Campus. We are not seeing an increase in PDA, which is good. And on top, we are generating a healthy financial revenue because of these average receivable term that is longer than in previous years.

And looking at Primary & Secondary education, you can see year-on-year an evolution of 12 days. Here, this is mainly due to a higher volume of book collection sales to our associated schools that are related to the first semester of 2016. A part of our sales to the first semester of 2016 occurred in December.

We are more efficient this year than last year and, therefore, the average receivable term increased. What we expect is that the average receivable term of the costs of Primary & Secondary education will converge until March 2016 to the levels that we see last year in 2014.

Now, moving to page 21, we can see CapEx, so our investments as in other quarters, we divide investments in recurring and special projects. So, looking on the left-hand side of the page, you can see on the quarter BRL 111.9 million in investments recurring in CapEx, 8.4% of net revenues. On the year 2015, BRL 342.5 million, which is 6.5% of net revenues.

If we add the special projects and greenfields in the year, we have a total investment of BRL 439.3 million, which is 8.3% of net revenues (3:11) investment that was made in a very restrictive year from a budget point of view. But nevertheless, we've made all investments that were necessary related to expansions, library, IT, but also strategic projects that are related to greenfields, new business learning centers, new academic models, so all strategic projects were also concluded (33:37) this investment that was realized in 2015.

Moving now to page 22. We can see net debt, we ended the period 2015 with BRL 404 million in cash and a net debt of BRL 633.5 million and here, I'm already including all financial debt but also tax liabilities and M&A payments and this represents about 0.29 times EBITDA. This is a very healthy level of net debt, very comfortable to the point that we have capacity in our balance sheet if needed to capture debt and to fund any inorganic movement that may occur in 2016.

Moving now to page 24, we present here our cash generation in the quarter and in the year. So, I think one important thing here and it's a very positive message, despite the BRL 725 million of FIES that were not repurchased in 2015, we were able to generate in the fourth quarter, about BRL 110 million of positive free cash flow from operation. And in the year, a total of BRL 633.6 million positive free cash flow from operations. This is very positive despite increasing the average receivable term of FIES. We expect in 2016, with the normalization of the repurchases and the payment of 25% of the amount that is due on FIES, that this EBITDA-to-cash level increases in 2016.

So, now I'll pass the call back again to Rodrigo for his closing remarks.

Rodrigo Calvo Galindo {BIO 17238232 <GO>}

Thank you, Fred. Let's go to the last part of today's presentation for my closing remarks, please. The new enrollment and re-enrollment process have already begun and should be concluded in mid-April. Our (35:48) at this time is that base of students will begin flat considering new enrollments and re-enrollments. Another thing that I think is important to mention is that this year, we are instituting (36:00) no fewer than 238 products, which are making very good product progress including those related to our organic growth.

In our greenfield project, we expect to inaugurate 100 new units in five years and of this total, we already have 43 requests for opening new units under analysis of the Ministry of Education and one greenfield already approved it in the city of (36:26) has already been operated and should be inaugurated by mid-year of 2016.

In the Distance Learning Business, we also received authorization from the Ministry of Education to open 232 new centers, which 150 to be opened already in the first half of this year. Since these 150 Distance Learning Centers were approved already in the middle of our student recruitment process, they will contribute marginally to new enrollments in this first semester of this year, but have excellent potentially for the coming cycles.

The other centers, the difference between 232 that was approved and 150 that was implemented in the first semester, we are planning to open in the second semester of this year. I also want to note that in 2016, we see new opportunities for efficient gains from the projects that generate benefits in 2016. But that should continue to capture efficiency gains in 2016. This included the rollout of the KLS 2.0 and the maturation of the operational research software, which are products that will continue to generate benefits for years.

Another important project is the rollout of the Strategic Sourcing Project. In 2016, new categories will be included, provide an even more cost-cutting opportunities to be captured. And last, another initiative with the potential to create value for the company is the Retention Program, which is a set of projects to improve the students' retention with Kroton. We see enormous potential in all of these projects and we are confident in this prospect, which leaves us comfortable that even in a reverse scenario, we will not suffer any margin compression.

As we announced it to the market, I should also mention here that we concluded the process to sell Uniasselvi with the first installment of BRL 400 million received in February. We also approved the distribution of dividend of BRL 70 million to ensure a constant flow of distributions to our shareholders.

In closing, I'd like to reinforce the point we highlighted last quarter, which is Kroton's excellent capacity to adapt. We have shown that the company is capable of generating value in the short- and long-term by overcoming adversities and delivering high quality education on a large scale.

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

Q&A

Operator

Ladies and gentlemen, we will now initiate the questions-and-answer session. At this time, we will begin with a question from Rodrigo Gastim of BTG Pactual.

Q - Rodrigo Gastim {BIO 19694950 <GO>}

Hi. Thanks. Good afternoon, everyone. I just would like to better understand what's behind the nice control in out-of-pocket receivables. I mean, the macro environment keeps deteriorating and it would be more than normal to already start seeing receivables base coming up.

So, my questions are basically, number one, what was the main drivers to keep it under control in Q4? And number two, if you expect it to remain at current levels during 2016? I mean, close to this 60 days of receivables, excluding FIES and excluding PEP as well. Thank you very much. That's my question.

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

Okay. Hi, Rodrigo. It's Frederico. Yes, you're right. I mean, everything that we see from external news is deterioration, it's a reality. But what I can tell you about Kroton, I mean, I think if you look mathematically why the average receivables are stable, we have two things. One is the gross accounts receivable that is under control and this is the result of a series of prevention, measures to maximize the payment on date, so our students have the due dates and we have a set of initiatives to maximize the number of students get pay on-date. And the second thing is the set of initiatives to improve the performance of our collections once the student didn't pay on-day, on-time. And here, we have a series of different initiatives, both on the more recent type of delinquency balances, but also on old balances across the board. So, we are able to keep stability on gross accounts receivable.

The second thing that is very important is the provisioning level. The net accounts receivable is the metric that we use for every receivables done. So, our coverage ratio today is high and is comfortable enough to the levels of PDA that we are seeing in our operations. So, the combination of the two result in a stability of our average accounts receivable term.

If we start decreasing PDA, these accounts receivable will increase or if we start receiving less, our accounts receivable will increase. So, as I mentioned on the call, there's a series of initiatives, the macro environment is tougher. But so far, we are able to mitigate the totality or almost the totality of the negative impact that we are seeing outside.

For 2016, I'm not going to provide any guidance right now in terms of evolution. We are alert and we are following our accounts receivable day-by-day. If needed, we will increase our PDA levels, if not needed, we'll not increase our PDA levels. But I cannot tell you right now if they will increase or not.

Q - Rodrigo Gastim {BIO 19694950 <GO>}

Perfect, Fred, that's very clear. Thanks very much.

Operator

And we do have a question from Ruben Couto of Itaú BBA.

Q - Ruben Couto {BIO 20636571 <GO>}

Good morning, everyone. Thank you for taking my question. I have two questions on the intake cycle that we are currently in. First on PEP, they don't seems to be – the two seems to be growing quite well, but thinking on the original reason that the company created this two, which was supposed to be a bridge loan for students that didn't manage to get FIES. I just wanted to get an update on how was – how it has actually behaved in the first batch of PEP students, those that got the PEP 90 Program? How they are managing? Did they manage to enroll in FIES? Are they dropping out beyond you guys expected? Just to get a sense if the whole idea on this bridge loan too is working as expected. And a second question is still on the intake cycle. How do you guys are seeing the FIES' conversion in the first half of 2016 compared to the second half of 2015? And thinking about all the restrictions that the government is implementing on the program, are you managing to improve on a half-to-half year basis, the level of conversion of the FIES that you managed to get? These are my questions. Thank you.

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

Hi, Ruben. It's Rodrigo speaking. So, for your first question, yes, you are right that our first installment product that it was effective then (44:15) that was offered in the first semester of 2015, it was a bridge loan. But these are only for the PEP 10, and it was exactly what we did. We offer PEP 10 for one year and all the students in PEP 10 was migrated out – after this year, was migrated for other installment solutions like PEP 30 or PEP 50, for example.

In the second semester of 2015, we implemented the PEP 30 and PEP 50 and these two installment projects was not a bridge loan. It was a special installment for all the course, for all the length of the program. So, we are very comfortable with the solution that we offer. The interest of the student in the second semester of 2015, it was a small, on a low part (45:03) of the new intakes came from a special installments. But now in 2016, between 20% and 25% of the our new intakes came from the PEP 30 and PEP 50. So, a very good trend that shows that we are providing a solution that is being used for our students.

About FIES, what we expected is a better conversion than last year. Last year, we had around 50% of conversion comparing the number of seats that we received from the Ministry of Education and a number of students that we did enroll. We delivered a little bit increase of this percentage, but we still don't know the process of (45:43) a lot of operational things that needs to be improved and we are working with the Ministry of Education to improve this operational things and we expect a little bit better conversion than we had in second semester of 2015.

Q - Ruben Couto {BIO 20636571 <GO>}

Great. Thank you for details, Rodrigo.

Operator

Ladies and gentlemen, 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>}

Once again, thank you for participation in today's call. And our IR is available for more questions. Thank you.

Operator

Thank you. This concludes today's presentation. You may now disconnect your lines. Have a nice day.