

Q3 2021 Earnings Call

Company Participants

- Marcela Bretas, Head of Investor Relations and Strategic Planning
- Unidentified Speaker

Other Participants

- Antonio Ruetten
- Carlos Gomez Lopez
- Ian White
- Kaio Prato
- Ricardo Buchiglia
- Titus Labarta

Presentation

Operator

Good morning, ladies and gentlemen, and welcome to the audio conference call of B3's earnings results for the third quarter of 2021. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session and instructions to participate will be given at that time. (Operator Instructions) As a reminder, this conference is being recorded and broadcasted live via webcast. The replay will be available after this event is conclude.

I would now like to turn the conference over to Marcela Bretas, Head of IR and Strategic Planning.

Marcela Bretas {BIO 21760051 <GO>}

Thank you. Good morning, everyone. Thanks for joining our call. This quarter was very important to B3, we had several important strategic advances over the last couple of months that I'd like to share with you. So in October, we announced the acquisition of 100% of Neoway. Neoway is one of the largest data and analytics and into artificial intelligence companies in Brazil. For this acquisition, we are paying R\$1.8 billion, and it's in line with our strategy to diversify revenues and look for companies that have attractive growth opportunities within what we consider to be a first adjacency to our core business.

Neoway reinforces our product development capacity and accelerate our go-to-market for data and analytics products. And we are hoping to obtain over the next few weeks, the necessary approvals to go on and close this transaction. So this transaction is subject to a shareholders approval, we've called for an ESM in early December, December 9th, and

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we hope you guys do join and participate in this meeting. And also we are pending regulatory approvals from both CVM and CADE, which is the antitrust entity here in Brazil.

Also in October, we announced an investment in a company called Pismo for USD10 million. Pismo is a techfin company that offers a platform -- technology platform in the cloud for financial services. It's a very interesting company and a very high growth one with differentiated product portfolio offering. And we think this acquisition will help us strengthen our relationship with a key supplier for future developments here at B3.

Finally, in October we also obtained the regulatory approvals from CVM and CADE to close the investment in Dimensa. Dimensa is the company of TOTVS that we invested in R\$600 million in exchange for 37.5% stake.

Also, as a highlight for the quarter, we have the issuance in September for bonds amounting to USD700 million with a 10-year tenure, and semi-year payment of interest in the amount of 4.125%. This issuance diversifies the three sources of funding and will provide funding for us to pay that schedule to mature in 2022. This issuance was -- B3 became the first exchange in the world to issue a sustainability-linked bond, that has two sustainability targets linked to it. The first one is the creation of a diversity index here at B3 by December '24. And the second one is to increase the percentage of women in leadership positions here at B3 to a minimum of 35% by December '26. With this new debt issuance, B3 reviewed its leverage guidance for the year from 1.5x to -- up to 2x EBITDA of the last 12 months.

Finally, I'd also like to highlight two important operational developments for us. The first one was the amendment of the corporate law here in Brazil that now allows for super voting shares to be issued by companies that are looking to IPO here in Brazil. This is an important development for the local capital market and will likely incentivize a number of companies that work consistently [ph] during IPO in other markets to list locally. B3 has actively participated in those discussions and think this is a very important development for the local market. Additionally, in the end of August, we obtained the approval from the central bank to go ahead and establish our receivables platform that is in trial phase as of now, and will likely be launched by year end.

Moving on to financial and operational results. In the third quarter of '21, we saw interest rates rising as a result of higher inflation, but even with this scenario, we saw growth in all of our segments revenue line. We have achieved record levels in terms of capital raising here at B3 with close to R\$50 billion been raised through 25 offers of which 17 were IPOs and 8 were follow-ons.

Year-to-date, capital raised through IPOs and follow-on has reached R\$127 billion here at B3. Revenues reached R\$2.5 billion, which is in line with what we observed in the second quarter of this year, and with what we have in a small increase versus last year. When we disconsider provision reversals that we had in the second quarter of this year and the third quarter of last year, revenues were 7% higher than last year, and inline with the second quarter. EBITDA has reached R\$1.8 billion, a 9% growth compared to third quarter '20.

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Moving on to highlights of volumes. In the listed segments ADTV for shares, for equities reached BRL31.5 billion in the quarter, almost 10% higher than what we had last year. And it's -- and 5% lower than what we had in the second quarter, which is explained partly by the seasonality that we usually observe during the vacation months of the northern hemisphere. In listed derivatives, ADV grew for all contracts in line with higher volatility that we observed in the market.

In our OTC segments, volumes were up -- revenues were up 11%. We saw funding instruments issuances rising 3%, mostly driven by time deposits and fixed income stock was up 10%.

In the infrastructure for financing unit, volume was up -- revenues were up close to 11%, driven by higher, stronger volumes of vehicle financing and also real estate financing activity.

In the technology and data segment, revenues were up 19%, driven by the number of clients that we have in our monthly utilization service, which are a reflection of a more active buy side industry here in Brazil. And we also saw an increase in data revenues driven partly by exchange rates.

With that, I want to open up for questions. Thank you very much everyone.

Questions And Answers

Operator

(Question And Answer)

Ladies and gentlemen, we will now begin the question-and-answer session from investors and analysts. (Operator Instructions) Our first question comes from Ricardo Buchiglia, BTG.

Q - Ricardo Buchiglia

(Technical Difficulty) and congrats on the results. I have one question here, in the past couple of years, we haven't seen turnover velocity for the equity business accelerating significantly, for several different reasons, but with our more challenging market environment that's required if that turnover decreased sequentially. I understand that there is a lot of uncertainty involved, but could you please comment on our view for how turnover should behave in 2022 compared to the leverage [ph] this quarter? Thank you.

A - Marcela Bretas {BIO 21760051 <GO>}

Good morning, Ricardo. Thanks for your question. It's a tough one to answer. You are absolutely right. Over the last couple of years, we saw a sustained increase in the level of turnover velocity here at B3. That is explained by several different factors. So at first, when the -- early 2020, when the pandemic hit that turnover velocity was driven mostly by

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volatility. But as volatility started to decline, we saw other factors coming in and playing a role in helping sustain higher than what we had observed historically in terms of turnover velocity.

So, one of the drivers of higher turnover velocity is more investors coming in our equity's business. So, this is a trend that started in 2019. We started the year with close to 800,000 accounts at the depository and we finished the year with BRL1.6 billion, BRL1.6 million, I'm sorry. So, this is something that was driven by a decrease in interest rate and since then this number has multiplied by almost five-fold. So, now we are running with close to 4 million accounts at our depository. New investors that come in they have an immediate impact on the increased -- the increase in turnover velocity here at B3. Additionally, we saw a sustained demand from especially local institutional investors, as they navigated a scenario where real interest rates were at its lowest points in Brazil ever.

So this sustained demand from both retail and institutional local investors over the last couple of years has encouraged several companies to come in and go ahead with their capital raising plans and then we saw a number of IPO and follow-on offers taking place at B3, both of which contribute to the increase of ADTV, both in the market cap line, as well as in the turnover velocity side of the equation. We are seeing sort of a shift in terms of ADTV from the sectors that we typically had a higher weight in the ADTV. Other new sectors starting to gain importance and those sectors such as retail, technology, et cetera, they typically come with a investor behavior that has a higher turnover velocity.

Also, we have worked and promoted a number of new products such as BDRs for instance, and ETF that have been major hits with our investors. So, to give you a sense BDRs in the beginning of 2020 they represented about BRL20 million in ADTV and now this number is closer to BRL400 million. Combined with ETF, we now have ADTV from these new classes of products that have gained importance over the last few months of adding up to almost BRL2 billion in ADTV.

And finally, I think it's worth mentioning that we implemented in February a new pricing table, this intermediary model that we've been talking about that incentivizes two classes of market participants that also might have an important impact on turnover velocity, which our retail investors by the exemption of the fees that they pay in our depository as well as day traders for which we are offering deeper discount for their transactions. So, if those two groups of clients -- if we are successful in our strategy and those two groups of clients increase the volumes that they trade here at B3, that also might play sustainable part in keeping turnover velocity at higher levels.

Finally, we just had this change in corporate law that I mentioned, allowing for super voting rights. We still have to wait and see what the impact of this will be. But potentially, theoretically what we could see is companies coming in with higher free floats in order -- in their IPOs and follow-on allowing in with higher free floats that also tends to have an impact on turnover velocity.

So with that, all I'm saying is that structurally we had some factors that played in to justify a higher turnover velocity. On the other side of the equation, what will have to balance is

the increase we are observing in interest rates and how this will play out over the next few months? So we'll kind of have to wait and see. Sorry, if I can't be more precise in my answer.

Q - Ricardo Buchiglia

No, that is great. Thank you.

Operator

Our next question comes from Carlos Gomez, HSBC.

Q - Carlos Gomez Lopez {BIO 19127284 <GO>}

Hello, good morning. Thank you for taking my question. First, I would like to know if you could give us an update on your legal contingencies, in particular the one is closed recently about the case coming back from 1999. We saw that you updated the amount and we would like to know if you have any news and when you expect the court to take the case and to issue a resolution if you have any new information?

And secondly, I would like to ask about the change in leveraging. I mean you have taken more you have changed the guidance. We're in the middle of an interest rate cycle, everywhere rates are going up. Is it's the right time for you to be taking on more leverage? Thank you so much and congratulations on the results.

A - Marcela Bretas {BIO 21760051 <GO>}

Good morning, Carlos. Thanks for your questions. So the first one if I understood correctly, you want to talk about the case from (inaudible) that we are now reclassification in last quarter.

Q - Carlos Gomez Lopez {BIO 19127284 <GO>}

That's correct.

A - Marcela Bretas {BIO 21760051 <GO>}

So this case -- yeah. So this case we have no news since then. I think it's probably going to be a while before we have anything to report on that front. Our lawyers' their best guess at this point it at it's likely going to take probably another three years, two to three years for us to have a trial, a new trial on this case. And it's unlikely that we'll have any news to report on that front in the near future? On the leverage front, I think here we -- there was -- we have some debt redemptions scheduled for next year. And I think one of the goals was to prepare ourselves ahead of an election year that is -- in the coming year we'll have elections and typically what we see in election years, it's a more -- probably a more volatile market that could impact our ability to raise funds at an attractive rate. So we wanted to anticipate ourselves in case that's now materialize and we wanted to take advantage of a good market conditions that we observed and prepare ourselves liquidity wise. And this increasing leverage should be temporary.

Q - Carlos Gomez Lopez {BIO 19127284 <GO>}

Okay. That's clear. All right. On the first case, sorry, on the legal case, can you remind us what the interest rate is accrued for the amount at risk?

A - Marcela Bretas {BIO 21760051 <GO>}

It's sort of an inflation index plus 6% a year.

Q - Carlos Gomez Lopez {BIO 19127284 <GO>}

Plus 6%. Okay. So, it's what the Sao Paulo court index?

A - Marcela Bretas {BIO 21760051 <GO>}

Yes. SPJ.

Q - Carlos Gomez Lopez {BIO 19127284 <GO>}

SPJ. Okay. Thank you so much.

A - Marcela Bretas {BIO 21760051 <GO>}

You're welcome.

Operator

Our next question comes from Ian White, Autonomous Research.

Q - Ian White {BIO 15068031 <GO>}

Thanks so much for doing the call. Just a few questions from my side, please. First of all on Neoway, I wondered, if you're in a position to provide any update on the synergy opportunities there at this stage. I think I remember from the call you had recently this was something you were still exploring and there maybe some guidance in the future. So, anything else that you could be said on that would be of interest, please. Secondly, can you help me understand, roughly what percentage of your revenue is inflation-linked? Is it substantially just the technology and data contracts or are there other areas where you have inflation linkages within pricing agreements, please? And finally, can you help me understand what has happened in other revenue within technology and data during the quarter? I think it was fairly healthy year-over-year growth, but sequentially step down about 28% versus 2Q '21. So just looking to understand what's changed there, please. Thank you.

A - Marcela Bretas {BIO 21760051 <GO>}

Hi, Ian. Good to hear from you. So on your first question regarding synergies arising from the Neoway transaction, we anticipate mostly synergies coming on the revenue front from potentially new products and leveraging on their established platform to accelerate our go-to-market for our data and analytics products. We are not providing at this time any guidance related to the level of synergies, yet. We are working on trying to detail these

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new initiatives that we could potentially develop in partnership with them. But at this point we're still waiting for the antitrust authority's approval. So, we are somewhat limited in the work that we can do and the level of granularity that we can have. So, we are working on putting together this plan and we'll detail this in over the last -- over the course of the next few months.

But as I said, we expect important synergies coming from the complementarity of the data that we both companies have B3 and Neoway. And from the platform that they already have in place as a distribution platform for our data and analytics products for B3, not only in for the credit and retail segments but potentially also for the data, for capital markets and financial services that we are working on.

Moving on to your second question, which was -- the second question can you repeat that? Sorry, Ian.

Q - Ian White {BIO 15068031 <GO>}

Yeah. Sure. It's just -- I was just wondering if you could help me understand roughly what percentage of your revenue is inflation-linked?

A - Marcela Bretas {BIO 21760051 <GO>}

Sure. So directly inflation-linked we have part of the technology mostly utilization line is typically annually, we adjusted by inflation, in our infrastructure for financing unit, he services that we provide for the SMG and the contract system typically also annually we adjusted by inflation. And in other segments, we have the indirect benefit from inflation in the sense for instance, for typically volumes could increase in the listed segments with more inflation, right? So as we charge our basis points fee on the volume that is trade or the number of contracts that is negotiated that will tend to capture some increase in inflation in some form.

Also in the OTC segment, we have the stock of fixed income instruments here at B3 being sort of adjusted by nominal interest rates. So this should also capturing some form and we charge basis points fee on this as well. So this sort of captured the increase of inflation as well. So I think, for most of our revenue lines, we are sort of protected from inflation in the sense that either volumes or prices will tend to grow at least with inflation. And finally, for your question Fernando will address your question on the other revenue line in the technology and data services.

A - Unidentified Speaker

So it's mostly about the services. So we have a drop in auctions that we have -- that we hold in B3. So we have a platform for options, there was less options this quarter. And fines which is we have a market participants doesn't comply with some rules about our settlements, we have a fine and there was a decrease in that also in the quarter, but it's not something that is relevant.

Q - Carlos Gomez Lopez {BIO 19127284 <GO>}

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Super. It's very clear, thank you.

Operator

Our next question comes from Kaio Prato, UBS Bank.

Q - Kaio Prato {BIO 20631854 <GO>}

Hello everyone, thank you for the opportunity for asking questions. I have two questions here, if I may please. The first is related to the average fees charged on the equity side. We saw a reduction again this quarter with the implementation of more incentives in June. Just I would like to have an update and understand if operation changes are all ready to be implemented now and what are you expecting in terms of prices for the following quarters?

And the second is related to the public hearing in CVM. Just wondering if you have -- if you expect any movement into the end of this year, or if you have any update on the timeline for this resolution, please. Thank you.

A - Marcela Bretas {BIO 21760051 <GO>}

Good morning. So, your first question -- I'll start by the second question -- about CVM, and the public hearing process. We do not have any insights in terms of timing here to share with you guys. So it will it's a completely up to CVM this question. So we unfortunately do not have any update to give on that front. Second question about the pricing for the equity segment, we as of now we have not implemented the full model that we intend to do, we are still working on it and it's still very much our intention to go ahead with the full model as soon as possible. But again, we are here not completely in charge of the timing of it. We are hoping to go ahead and complete the full model as soon as possible, hopefully over the coming few months.

On regards to potential price's fluctuations you might see, it's sort of the characteristic of this new pricing table that margins will adapt and adjust according to volumes. So in a quarter in which you see higher volumes, you probably will typically see an average lower ticket and vice-versa. So this pricing might fluctuate, and it's sort of the nature of the new pricing scheme that we are implementing.

Q - Kaio Prato {BIO 20631854 <GO>}

Okay. Thank you. Just a follow-up on this, just to have the full implementation, what is missing on your side today?

A - Marcela Bretas {BIO 21760051 <GO>}

So in order to have the full implementation, it is required that all market participants make some adjustments to their systems. So that's we are -- it's an ongoing process, those are the patience [ph] and once it's finalized, then we'll be able to implement the full model.

Q - Kaio Prato {BIO 20631854 <GO>}

Okay. Great. Thank you very much.

Operator

Our next question comes from Titus Labarta, Goldman Sachs.

Q - Titus Labarta

Hi, good morning, Marcela. Thanks for the call. A question on the goodwill lawsuit, you released a notice to the market during the quarter in 2017 potential financing BRL240 million. Just to understand -- or BRL204 million. What is the impact or is the potential tendency on that one? And then just on the total goodwill lawsuits, what are the potential if you can just kind of remind us the total potential financing from the Google lawsuit. And then there was another one related to the tax rate for the CME also about BRL1.1 billion. You can give us what is the potential risk there, do you provision anything for that? Could just give us an update on that as well? Thank you.

A - Marcela Bretas {BIO 21760051 <GO>}

Hi, Titus. So this new goodwill notification that we received from the IRS is a total of close to BRL200 million. It's just basically, just penalties, because for the time period to which it relates, we actually had a net loss. So we hadn't compensated in that quarter any gains with the tax shield from the goodwill. So it's basically just a penalties and it amounts to close to BRL200 million. The upstanding cases that we had prior to this, they amount to close to BRL12 billion. And so that's sort of where we stand and no new development in the other cases that we have outstanding. So, Fernando will talk a little bit about the CME case.

A - Unidentified Speaker

Hi, Titus. So the CME case, we had a stake in CME, about 5% of CME. So we saw that a part of that in 2015 and some part of that in 2016. So the case that we are discussing now, it's a case of -- in the 2016. So it's about the FX variation on the investment that we had. When we sold our stake in CME, we recognize a gain and this gain we included the FX variation, which was favorable to us. So the IRS is disputing that with us and we are more than confident that we are going to also win this case because we did everything is strictly by the law. We couldn't do any other way. So we just recognize these effects that fluctuate variation on the investment. And we recognized that when we were paying the taxes. So that's about it. We had another case, this is about the 2016 case, the 2016 sale and 2015 sale is also disclosed in our reference form. So, if you want to check it out, it's there.

Q - Titus Labarta

All right, thanks Marcela, Fernando. And so, just on that CME, I think it was BRL1.1 billion, right? That's a potential penalty that you don't think you're losing.

A - Unidentified Speaker

Yeah. No, we don't. We are pretty confident that we are also going to win this case.

Q - Titus Labarta

Okay, great. Thank you. And maybe just one question on the receivables market, I think you said -- just remind us, when do you expect to start and I know there has been some several issues there, I think, on the interoperability and settlements transactions. Do you think that that will be a concern for you as you enter that market? How comfortable are you that those issues will get resolved? And what is that a potential upside that you may see for you in terms of your revenues that may come from that? Thank you.

A - Marcela Bretas {BIO 21760051 <GO>}

Titus, we are in the pilot test phase of our platform, our intention is to launch it by year-end. I think, we are pretty comfortable with the stage that we are in. In terms of interoperability and how the platform is working, I think the market seems to have overcome the technical difficulties that we had in the past. For us, it could potentially in the future become an important revenue opportunity, but it's likely that it's going to take some time to build volumes over there. So, we are at this point as you know we don't disclose guidance in terms of what we see as revenue potential, but -- and this will probably likely be a gradual process of built-up, but we are optimistic about the potential size of this market in the future.

Q - Titus Labarta

Okay. Thank you, Marcela.

Operator

Our next question comes from Antonio Ruetter from Bank of America.

Q - Antonio Ruetter {BIO 20857460 <GO>}

Hi, Marcela. Thanks for the call. So my first question here is on revenue diversification, if you could comment on the multiple business lines that you are adding. And if you have appetite for further M&A as you could see, especially on data and just short to mid-term after Neoway. And second question, if you could comment on the behavior of the retained investor steady strong addition in traders over next years -- over the last years. How did they behave over just the last three months with greater macroeconomic uncertainty especially in Brazil? Thank you.

A - Marcela Bretas {BIO 21760051 <GO>}

Good morning. Thanks for your questions. So starting with the strategic view that we have on Neoway transaction and overall our strategy to expand, after the merger between BM&FBOVESPA entity back in 2017, we designed medium term strategic plan for B3 in which we decided that there were basically two pillars for our strategy going forward.

The first one was to strengthen and maximize the potential of our core business. And the second one was to selectively look for growth opportunity in what we consider to be first adjacencies to our core businesses diversifying our revenue streams. So, the acquisition of Neoway is in line with the second pillar as well as is the case for the investment in

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Dimensa. So in these two cases what we saw were markets that were very close to our core business, serving potentially very similar clients and offering new products that we see a great growth potential going forward.

So data for sure, data and analytics it's an important avenue for us to pursue in terms of future growth as you probably see other exchanges around the globe have been very active in growing their data revenue lines. It provides a new source of revenues that is typically less transaction oriented and it's high growth. So we think that in these three we have very unique data that we could lever on and offer products to the market that could really add value to our clients' credit activities, their assertiveness in their sales and marketing efforts, in their KYC, AML practices. So we think those products could really add value and that could be a very strong demand for this. So, definitely data is an important avenue of growth that we wanted to pursue.

And we have several organic initiatives within B3 in line with this strategy, and eventually we might consider doing M&As when we think that this will either bring us an expertise that we don't have in house or provide a faster go-to-market or bring in complementary data or help us in our product development efforts. So that's what we did with in the case of Neoway.

Moving on to your question relating to volumes and if I'm not -- if I understood correctly you're asking about the volumes of day traders in a scenario where you see more volatility, was that is?

Q - Antonio Ruelle {BIO 20857460 <GO>}

Yeah. Especially in Brazil we have certain macro and B3 added a lot of investors over there -- over the last years. So, how are they behaving now?

A - Marcela Bretas {BIO 21760051 <GO>}

So for now we continue to see an increase in the number of both retail and day traders here at B3. As we disclosed the number of accounts, depository grew 4% sequentially. So we continue to see this trend laying out despite the scenario of higher interest rates.

Q - Antonio Ruelle {BIO 20857460 <GO>}

Okay. Thank you.

Operator

(Operator Instructions) This concludes today's question-and-answer session. I would like to invite Marcela Bretas to proceed with her closing statements.

A - Marcela Bretas {BIO 21760051 <GO>}

Again everyone thanks so much for your time and for listening to our call. Your continued support to B3 is very important to us. The full IR team is available if you have any follow-up questions, we will be glad to talk to you. Thanks so much and have a nice day.

Operator

That does conclude B3's audio conference for today. Thank you very much for your participation. Have a good afternoon and thank you for using Chorus Call Brazil.

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